THE CORRECT ECONOMY FOR THE MACHINE AGE

BY

A. G. McGREGOR

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WITH A FOREWORD BY

JOHN A. HOBSON

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FOREWORD

By JOHN A. HOBSON

Among the many business men engaged in the discussion of the Great Depression and its remedy, Mr. McGregor stands unique, both in his intellectual grasp of the problem as a single whole, and in the courage and logic of the policy he advocates.

Most business men visualize the forest from their own particular tree by a process of short-sighted and illicit generalization. Mr. McGregor takes a wider and more objective view of the situation. He sees healthy progress in industry in terms of true balances between full production and full consumption, both within each nation and in the world economy. Unemployment of labour and capital must be overcome.

In closely-reasoned chapters he sets out the root causes of that lack of balance which is exhibited in every country in the shape of under-production and under-consumption, and relates this national lack of balance to the international disturbances which have driven each nation into policies of narrow economic restriction so damaging to free trade intercourse and so wasteful of world resources.

The increasing capacity of production, taken in conjunction with the policies connected with a gold basis of exchange, has given a size, a duration, and special character to our Great Depression. But the whole trouble is rooted in a maldistribution of

purchasing power, which incites attempts to over-save, over-invest, and over-produce, and the only sound permanent remedy is to be found in measures which shall give wage and salary earners a share of the total income adequate to raise their demand for consumption goods so as to correspond with the increasing powers of production.

This cannot, Mr. McGregor argues, be achieved either by a wasteful struggle between groups of employers and employed in the several trades, or by a general displacement of private initiative and competition under State Socialism. The disappearance of capitalism is neither practicable nor desirable. But, in the process of redistributing purchasing power so as to restore and maintain the just balance between productive capacity and consumption, the State, as representing the interests of the whole community, must play an important part. Wages and salaries must be raised in the whole industrial system.

Now this policy, though advantageous to capital as well as labour, cannot be achieved by individual firms or individual trades which stand to lose if they act alone. It can only be achieved by the common simultaneous action of the whole economic community. For only thus can each business and each trade realize that its higher labour costs will be more than compensated by a fuller use of its capital, and a larger, reliable consumer market at a higher price level.

If every business man knows that all others in his trade and every other trade realized and would

act upon this sound economy, State action might not be necessary. But this is an impossible assumption. Hence, Mr. McGregor is driven to a proposal which may shock and disconcert many of his readers until they come to realize its necessity, viz. that the State shall decree a given rise in wages and salaries to take effect on a given date. The delicate task of adjusting the amount of the rise to the condition of the several trades is to be entrusted to a Commission upon whose competence and fairness a great deal must depend. But a higher and a fairer rate of wages is essential, and its achievement cannot safely be left to futile struggles within each trade. Therefore, however difficult this procedure by a national decree may be, the difficulty must be faced, and Mr. McGregor puts forward the index which should govern the rises in wages.

Not less radical and important are Mr. McGregor's proposals for dealing with foreign trade and investment. He argues that each nation can and should maintain, by regulated monetary action, a true balance in its import and export trade.

Under the old order, where the excessive profits from low-paid labour were driven into foreign investments, great trouble arose when payment of interest was required, either in gold, which upset the whole monetary system, or in goods, which reduced home production. Under existing conditions, when this policy of foreign investment is common to many industrial countries and is visibly responsible for unemployment, free individual investment can no longer be tolerated. Control of foreign investment

within each nation must be exercised by some central bank, or better still, by an International Clearing House.

Mr. McGregor's full and close discussion of the operation of such a Clearing House forms one of the ablest and most original parts of his constructive proposals. He does not deny the difficulties attending such a delicate process of international co-operation, holding that the necessary faith will only be achieved by perceiving the greater difficulties attending separate national exchange controls.

There are three conspicuous merits in Mr. McGregor's economy: First comes his powerful grasp of the conditions essential for a true balance between productivity and consumption. Second, his appeal not to idealism or altruism, but to an intelligent grasp of long-range self-interest among capitalists and employees. Third, his strong realization of the fact that the competitive system of industry is unworkable on pre-war methods of finance. His is an appeal to reason and a belief that as business is normally conducted in its details on reasonable calculations of gain and loss, this process can and must be applicable to the wider, longer scale and more general conduct which the new industrial and financial interdependence in the business world demands.

Idealist reformers who would like to see a completely planned system from which individual initiative and competitive gains are eliminated will boggle at some of Mr. McGregor's assumptions. But they would do well to read his book before rejecting his account of the "correct economy."

I think his arguments will win a wide acceptance among thoughtful business men, economists, and politicians as soon as they get over the first shock of a compulsory all-round rise of wages and salaries as a prime condition of recovery and continued prosperity.

J. A. HOBSON.

PREFACE TO THIRD EDITION

No country is making any noteworthy progress in permanently solving its unemployment problem and some countries believe that the solution of their economic difficulties is to be achieved by increasing their free trade area through the expansion of their own domains—a view which unquestionably increases the danger of war. National and international unrest is ruling because of grossly faulty economics.

The gravity of the situation has impelled the author to add materially to his book in an effort to prove conclusively the following points—

1. Each country desires and should have a consuming power in step with its full potential productive power, and would be constantly enjoying this desirable end if it would merely put its own economic house in order.

2. Depression rules because we have failed to recognize the transcendent economic importance of wages in the Machine Age. The buying power of our money and the balance between our power to consume and our power to produce depends upon wages.

3. There can be no worth-while prosperity at the present stage of industrial development while wages, the most vital economic factor in the welfare of all, are adjusted by a method so crude as the "dispute method."

4. There is a clear and logical index to which

wages, and salaries in the lower brackets, must always be adjusted if the best interests of capital as well as labour are to be served.

5. Competition is the life of trade. Allowing profit without competition means privilege and is the road to discord, revolution, and dictatorship, with the loss of economic and civil liberty.

6. Free trade with all the world would prove far more advantageous to the people of every country than territorial expansion.

7. Any country can quickly enjoy the benefits of free trade if it will practise a correct exchange policy.

8. There is an international exchange system which will ensure free trade to every country always in harmony with its own best interests and which is bound to become the future system.

9. Prosperity under free trade and without any entangling alliances is the stepping stone to lasting world peace.

10. Reverence for inflexible exchange rates and the quantity theory of money for controlling prices is orthodox fog which must be cleared away before any worthwhile prosperity and lasting world peace is possible.

A. G. McGREGOR.

LONDON, *May*, 1936

CONTENTS

CHAPTER I

INTRODUCTORY

CHAPTER II

CURRENCY UNIT OF CONSTANT PURCHASING POWER AND ITS ADVANTAGES

CHAPTER III

HIGHER PRICE LEVELS AND PROSPERITY

CHAPTER IV

GOVERNMENT ASSISTANCE

CHAPTER V

ECONOMIC POLICIES OF GREAT BRITAIN SUBSEQUENT TO THE OUTBREAK OF THE WAR

CHAPTER VI

ECONOMIC POLICIES OF THE U.S. SUBSEQUENT TO THE OUTBREAK OF THE WAR

CHAPTER VII

BANK CREDIT: ITS USE AND CONTROL

CHAPTER VIII

CORRECT EXCHANGE POLICY FOR A NATION ACTING INDEPENDENTLY

CHAPTER IX

INTERNATIONAL CLEARING ASSOCIATION THE IDEAL FOR INTERNATIONAL EXCHANGE AND LIQUIDATION OF INTERNATIONAL DEBTS

CHAPTER X

INTERNATIONAL INVESTMENTS

CHAPTER XI

LASTING WORLD PEACE—CONCLUSIONS

APPENDIX

THE CORRECT ECONOMY FOR THE MACHINE AGE

CHAPTER I

INTRODUCTORY

JUST as the last war is known as the Great War, so will the present depression go down in history as the Great Depression. The present depression will be the last because it will continue until we learn to make use of the correct means for overcoming it, and having learned the use of that means we utilize it to prevent another.

The causes of the present depression are often ascribed to one or more of the following: too many machines, too many workers, hours too long, profits too high, not enough Government spending of borrowed funds, not enough workers on the farms, etc. The truth is that none of these is responsible for the depression, and to change any of them would be merely treating the symptoms and not the cause of the depression.

The primary cause of the depression in each nation was the fact that its consuming power fell out of balance with its productive power. The depression continues because the gold standard economy, the *artificial* means by which former depressions were overcome, is no longer applicable, and because in our efforts to treat the effects of depression we are using

means which obstruct the natural attraction between idle capital and idle labour. If we would treat the cause which obstructed this attraction in the first place, and stop doing those things which continue the obstruction, we would find that our supply of workers and machines is inadequate for the demand and that wages and profits were not nearly high enough. Also we would find that tax rates could be materially reduced, Government spending of borrowed funds for affording unemployment relief could cease, many of the workers on the farms would take employment in other industries paying much higher wages, and we would find that a 44-hour working week would not be too long in most industries to produce the quantity of goods and services needed and desired.

The belief is common in each country that it has a power to produce much beyond its power to consume, whereas no nation can ever produce by the most efficient organization possible the equivalent of more than its people would like to produce and consume. If our economy functioned naturally and in harmony with man's nature there would always be a shortage of labour and capital to produce, on the whole, the goods and services for which there would be a firm and ever-increasing demand. Labour would be in demand at much higher wages, and capital at much higher interest rates and profits, and each worker would be able to pick and choose his employment, and each capitalist able to pick and choose the employment for his capital—economic liberty would rule.

The trouble is that one interest proposes a treatment for its particular ailment which would harm other interests, forgetting that its prosperity depends upon the prosperity of all. By probing deeper it would be found that all our ailments spring from the same cause, and that if the cause were correctly treated prosperity for all would follow as a natural consequence.

This chapter is devoted to outlining the cause and cure of depression. The reasons for the suggestions made, and the machinery for carrying them out, are developed in greater detail in subsequent chapters.

As prosperity depends upon maintaining a balance between the power to produce and the power to consume, it may be appropriate at the outset to consider the relative magnitude of these two factors in our economy as it exists to-day.

The Capacities to Produce and Consume.

The Brookings Institution of Washington completed a detailed survey of these two factors as they existed in America in 1934. Conclusions from its "America's Capacity to Consume" follow:

1. "*During the so-called 'new era' of the gay twenties the United States was not living beyond its means* . . . The facts show that we actually produced more in 1929, for example, than was consumed, and that we might readily have produced, with the existing resources, plant and equipment, and labour supply, and without improvement in methods, approximately 20 per cent more than we did produce. We were not living on our capital, that is, using it up

without replacement; on the contrary, we made, throughout the decade of the twenties, large annual additions to the capital supply."

2. "*There has been a tendency, at least during the last decade or so, for the inequality in the distribution of income to be accentuated.* That is to say, while the incomes of the masses of the people were rising during this period, the incomes of those in the upper income levels increased with greater rapidity. Since the proportion of the income that is saved rather than expended for consumption purposes rises rapidly as higher incomes are realized, there has been a tendency for an increasing proportion of the aggregate income of families and individuals to be directed into investment channels."

3. "*Vast potential demands alike for basic commodities and for conventional necessities exist in the unfulfilled wants of the masses of the people, both rural and urban* . . .

"The unfulfilled consumptive desires of the American people are large enough to absorb a productive output many times that achieved in the peak year 1929. Even in lines of basic necessities great wants among the masses of the people still go unsatisfied. The trouble is clearly not lack of desire but lack of purchasing power."

4. "*The United States has not reached a stage of economic development in which it is possible to produce more than the American people as a whole would like to consume* . . ., it would seem to be evident that we have not as yet reached the age of abundance of which we all like to dream, and that extensive leisure

has not as yet been forced upon us as an alternative to a surfeit of goods and services."

5. "*We cannot materially shorten the working day and still produce the quantity of goods and services which the American people aspire to consume* . . .

"In due course we can expect a much larger production for the same expenditure of human energy than has yet been possible. But for the immediate future we cannot count on production taking care of itself if the working week is materially reduced. In any event, we are desirous of raising the standard of living substantially above the level hitherto realized—not merely restoring it to the unsatisfactory level then prevailing."

6. "*In emphasizing the need of increasing consumption, we must not forget the necessity of simultaneously expanding production* . . . The prevalent notion that the problem of production has been completely solved has led many people to conclude that *all* we need to do to remove our economic difficulties is to increase, by some means or other, the money income of the public—that nothing else is of any importance.

"No matter how much we may increase wage rates with a view to expanding purchasing power, we will not find available in the market places the goods which minister to the satisfaction of human wants unless they are produced."

The above conclusions, based upon conditions in the U.S., are applicable to other countries as well. The desire to enjoy higher standards of living is not peculiar to the American people. It is a strong natural instinct in all mankind, which will not be

satisfied in any country for many generations to come, and it would be impossible for any country to achieve a productive power beyond the need and desire of its people to consume.

Why the Depression?—The Way to Overcome it.

If the standard of living in America was at an "unsatisfactory level" in 1929, why has it been at a much more unsatisfactory level ever since? Why do so many who crave work and a higher standard of living remain in idleness and despair amidst idle facilities capable of producing the things they want?

Why is depression ruling in every country?

Depression rules whenever the capacity to supply goods exceeds the demand. In all the many previous depressions it was claimed, just as now, that there was too much machinery and that man's ability to produce had outrun his ability to consume. Yet a demand for goods was always brought about that put the unemployed labour and capital to work again.

To free ourselves from the present absurdity of want in the midst of plenty, we have merely to bring the demand for goods into step with the capacity to supply. The demand for goods and services can be brought into step with the capacity to supply only if all of the returns from production are made available for consumption. To make *all* of the returns from production available for consumption there are three methods, but only three, from which to choose—

(*a*) *Investing savings abroad for which there is no employment at home, and thus financing foreign*

buying power for the surplus products. This method was practised for many decades prior to the War. During that period Great Britain was an exporting nation, but by receiving incomes in the form of goods from those foreign investments, she has become an importing nation. As foreigners are having difficulty in meeting their present obligations to British investors, and as incomes from foreign investments must be paid in goods, and later tend to increase the excess of goods imported over those exported, foreign investing as a means of restoring balance between consuming power and productive power is not promising now.

(*b*) *Making all unemployed savings available for Government spending by borrowing or taxation.* The system practised during the War affords a good example of the way this method operates to keep the power to consume in balance with the power to produce. Because of the burden of existing debt, largely contracted during the War, the financing of more Government spending by borrowing, or higher taxes, is not attractive now, and, for reasons which will appear in Chapter VI, is unsound.

(*c*) *Paying wages and salaries on a scale that will ensure buying power at home for the bulk of the goods produced and all foreign goods for which the remainder are exchanged.* This method has had more application in the U.S. than elsewhere. While it functioned there in a limited and haphazard way, sufficient experience was gained to demonstrate that it has *very important advantages to capital as well as labour*. Through the combination of method (*a*)

and rises in wages commencing in 1922, dollar prices quickly rose and confidence was restored. Advances in wages happened to continue more or less in unison with the improvements in the methods of production, and were responsible for the unusual degree of balance between the power to consume and the power to produce which ruled in the years 1923-1929. High profits were made through low profit per unit of output and high volume of production. Although labour-saving machines reduced the labour required for producing a commodity, higher wages increased the cost of production per worker and increased the workers' consuming power, with the result that wholesale prices and employment remained fairly steady. Unfortunately, however, wages were not advanced enough. If wages had been higher there would have been consuming power at home for all that could have been produced, and wholesale prices would not have started weakening in the U.S. in 1926, and there would have been full employment at home for all savings. If the vast U.S. investments abroad during that period had not been allowed, the strain on the gold standard with the fall in the gold prices of commodities, which was largely due to the attempts to service those investments, would have been avoided.

During that era of prosperity in the U.S., industry was particularly free from price fixing and "combinations in restraint of trade," and to make profit a concern had to keep abreast of the times. Many small businesses grew into large ones, while others less efficient were closed down, not so much because

profits were reduced, as because the owners could make higher incomes with shorter hours and less worry as employees of larger and more efficient concerns.

Supply and Demand under Free Competition.

When the demand for goods is in step with the supply, and all are comfortably employed, complaints of the operation of the law of supply and demand are seldom heard, because it is through free competition that capital most effectively finds its way into pursuits which raise the standard of living, and that individuals enjoy the greatest freedom in the choice of their way of life, and most effectively serve themselves and society.

When the supply of a commodity exceeds the demand under free competition, its price falls until its supply comes into step with the demand. On the other hand, when the demand for a commodity exceeds the supply, its price rises until the demand for it is balanced by the supply. In this sense the law of supply and demand serves as a most useful regulator for keeping the supply of a commodity in balance with the demand. In this sense the action of the law of supply and demand, under free competition, is ideal, and to improve upon its free and orderly operation from the standpoint of the best interests of all would be an impossibility.

However, when we have the combination of free competition and a supply of goods in a nation in excess of the buying power for its goods, we have a condition which would quickly bring disaster in the Machine Age, if no *artificial* means were resorted to

for preventing the effects which would naturally result from such a combination.

Whenever the power to produce in a nation has fallen out of balance with the effective power to consume, some artificial means has always been required to prevent prices and wages from falling almost to nothing.

Ordinarily when the power to produce exceeds the buying power for goods workers are discharged, which further reduces the buying power for goods, and if no dole or artificial measure that thwarts the free operation of the law of supply and demand were resorted to, workers would take lower wages rather than starve. Prices, wages, and employment, would follow each other down the slippery spiral almost to the vanishing point. Debtors would lose their equities to their creditors, and most of the workers would have to return to the land or starve.

In previous depressions the link of the currency unit to gold *has been the artificial means* which prevented such a catastrophe. When the consuming power for a nation's goods got out of balance with its productive power, employment, wages, and prices in terms of gold, followed each other down the spiral until a price level was reached that attracted buying from gold standard countries which were not in depression. The foreign buying gave confidence that the bottom had been touched and that prices would tend to rise and that better trade could be anticipated by the distressed nation. Also foreign investing, which finances foreign buying power, generally played a part in restoring equilibrium

between consuming power and productive power, but as will be shown later it was harmful to the subsequent best interests of the investing nation.

The gold standard, as it operated prior to the War, was helpful in preventing a complete standstill in the industrial activity of a country when its productive capacity exceeded its effective consuming power. But its action was slow, and the slide down the vicious spiral was not even checked until after many debtors had been ruined, and there was a large amount of unemployment and suffering generally, and the progress out of that condition was slow. In the present depression the gold standard was so wrecked by international investments, war debts, doles, inflexible wage rates, and tariffs, that it was no longer effective in preventing a collapse of prices and employment. We can no longer depend upon foreign buying through the operation of the gold standard for preventing the ill-consequences of productive capacity in excess of consuming power.

On the other hand, when a nation's buying power exceeds its productive capacity a little, as it has at times when, for instance, Governments have handed out claims for goods in the form of "printing-press money" in excess of the supply of goods, prices and wages have soared. This is a condition which brings serious harm, and is to be avoided also.

The law of supply and demand is a blessing to a nation if demand, on the whole, is in step with supply, but it is a curse to a nation if supply, on the whole, exceeds demand. To reap the greatest benefit a nation must allow a free operation of the law of

supply and demand in so far as it affects individual commodities, but it must provide the logical means for keeping its consuming power in step with its productive power. To attempt beyond this to improve upon supply and demand for "economic planning" would be painting the lily.

Free Competition should Not be Stifled.

Because of the action of free competition when consuming power is out of balance with productive power, there is a growing disbelief in its merits. In fact there is now a widespread belief that the balance between consuming power and productive power is to be achieved through curbing economic liberty. Therefore before discussing the simple and only possible means by which the present deplorable unemployment situation may be quickly and permanently overcome, it may be well in passing to point out that *without economic liberty* the problem of finding useful employment for all, and the problem of ensuring equity between capital and labour, and between the capitalists themselves and the workers themselves, are impossible to solve. Any plan for overcoming the scourge of unemployment in which economic freedom cannot be relied upon to enable the individual to find for himself the nook in which he can best serve himself and society, is doomed to disappointment.

Useful employment for all in our complex organization of society never has been and never can be brought about without a strong attraction between idle capital and idle labour, a condition which is

natural, but which cannot rule if economic freedom, which is also natural, is restrained.

Competition is the life of trade. When trade is deprived of its energizing force, as it is when production is allocated or when prices are fixed by agreement, the necessity for an employer to be on the look out for better and still better methods is removed, and his incentive to install better tools and thus give employment to capital and labour in the production of producer's goods is greatly reduced if he cannot underbid his competitors in order to increase his volume of production. Consequently his opportunity to satisfy his need for more profit is confined mainly to working his employees harder and reducing employment, or reducing their wages, either of which reduces buying power.

Thus when free competition is stifled inefficiency is stabilized, the great essential for overcoming unemployment—the attraction between idle capital and idle labour—is weakened, the conflict between capital and labour is intensified and *prosperity is impossible.*

What the Government Should NOT Do.

Unfortunately we are trying to treat the many involved symptoms of depression instead of removing the cause. We are barking up the wrong tree and we hear complaints against free competition on every hand: "There must be more price fixing and quotas in the production and marketing of goods; there must be Government planning and supervision of industry; there must be subsidies, higher tariffs, shorter working hours, more workers on the land," etc.

Such measures stifle competition and do not promote a strong natural attraction between idle capital and idle labour without which prosperity is impossible, and *their practice constitutes the economy for continuing the depression.*

Government help in one industry calls for relief measures in another; and the seeming need for Government responsibility in industry is constantly increasing in the present depression. If we do not soon recognize our folly and about-turn and practise the economy for prosperity, the economy for depression will be carried to its logical conclusion. Before we know it, we shall be enslaved by bureaucratic domination of industry and regimentation, with division of responsibility, inefficiency and little satisfaction to anyone, except possibly to the more gangster-like politicians and their henchmen.

To enjoy the highest standard of living, that class of society, employed and unemployed, which derives buying power for goods through tax levies on the producers and distributors, but which gives no goods in return, should be kept reduced in number to the barest minimum consistent with the public good. While that class of society would be materially increased if we were to have the misfortune of losing the benefits of free competition, that handicap would be small compared with the loss of freedom to fend for ourselves.

What the Government Should Do.

Through forces generated by competition, but by many ups and downs, we have been advanced into

the Machine Age. Because of the "downs" many advocate adopting some other system, whereas if we are to reap the maximum possible benefits we should merely eliminate the "downs" and allow a freer operation of the forces by which we have been advanced.

Before abandoning free competition, which has such tremendous advantages, we should search for the cause which brings about the maldistribution which is so disastrous to prosperity. Then if we find that the Government, by rendering a simple service, could preserve a balance between the power to consume and the power to produce under free competition, we should *ask the Government to perform that simple service* rather than ask it to take on the endless responsibilities it is ill-suited to perform, but which it must attempt to perform if we are deprived of the very important advantages of economic freedom.

Free competition is a fundamental requirement to economic liberty. The instant a Government sanctions interference with supply and demand, economic liberty commences to be superseded by privilege.

To interfere with economic liberty stabilizes inefficiency, weakens the attraction between idle capital and idle labour, continues unemployment and the need for doles for both, and brings the need for bureaucratic control of industry. Interference with economic liberty is the road to discord, revolution and dictatorship. Endless responsibilities fall upon the Government which, for the best interests of all concerned, would a thousand times better be left to the free operation of supply and

demand if the Government would merely assume responsibility for enabling demand on the whole to keep step with supply.

Because the balance between consuming power and productive power has been lost there is vast unemployment of both labour and capital—employment or unemployment for the one means the same for the other. The belief is prevalent in many countries that they cannot consume all that they can produce with healthy profits for capital—a more fallacious and a more dangerous belief to the well-being of a country in the present stage of industrialization is hardly possible. The idea that under any circumstances capital and labour need lose the attractions for each other that would ensure full and profitable employment for both is erroneous in the extreme.

Instead of interfering with free competition to prevent the consequences of lower prices and lower employment chasing each other in a vicious circle when consuming power is out of balance with productive power, the Government should merely concern itself with restoring the balance. *This is the simple change which must be effected in our economy if we are to enjoy the fruits possible to all in the Machine Age.* The Government should concern itself with the cause of the disequilibrium, not with the countless effects and symptoms.

A better economic combination than economic liberty and consuming power in step with productive power is impossible. Only through free competition and a balance between consuming power and productive power can there be the strong natural

attraction between capital and labour that will ensure useful employment for all who desire it.

Over-production and the Cure.

Whenever under the system of the past, we have been fortunate enough to get into a period of high prices, free competition has brought about an irresistible attraction between idle capital and idle labour, which continued as long as prices stayed up. Under free competition high prices stimulate greater and more efficient production, and later more goods start coming into the market than for which there is buying power. We have over-production, and under free competition prices start falling. Employers lay off workers and reduce wages and all costs as far as possible, and thus reduce the buying power for each other's goods. Prosperity is replaced by the misery of depression.

Over-production results from too much saving for investment in capital goods:[1] machinery, factories, etc., and not enough spending for consumers' goods: food, clothing, fuel, household goods, automobiles, amusements, etc. When over-production and falling prices become imminent the remedy is to save less and consume more. As the greater part[2] *of the total*

[1] The acute unbalance between consuming power and productive power which resulted in crisis and depression was generally precipitated by a monetary authority who, in his zeal to make the gold standard—a most fallacious instrument—serve as a basis of international exchange, contracted the bank-credit available to commerce below the amount needed for its normal transactions at theexisting price level. The rational control of bank credit is dealt with in Chapter VII, and the rational exchange system in Chapters VIII and IX.

[2] In one of his speeches, President Roosevelt stated that 90 per cent of the consuming power is ultimately in the hands of wage and salary earners. Exaggeration can be allowed for without impairing the argument in

consuming power is ultimately in the hands of wage and salary earners, higher wages and salaries are the remedy for over-production. Higher wages and salaries would provide greater buying power for the increased production, and would increase the costs of production. Both effects would tend to harden prices and preserve equilibrium. Employment for capital and labour would be maintained, and thus the best interests of both would be safeguarded. Capital might have to be satisfied with lower profits for a time, but lower profits would be preferable to serious unemployment of capital for a longer time. The lower profits for a time, and the higher wages, would be merely the correction of the unhealthy relation between profits and wages, which had been ruling previously.

When over-production and falling prices are imminent, higher wages and salaries for the consuming masses are the remedy, but under free competition for one or several employers to raise wages, acting independently, would be suicidal. If, however, they and all their competitors, and all other employers throughout the country, raised wages and salaries by the same flat percentage, the difficulty would be removed. *All must raise wages together to avoid individual injury and to derive collective benefits.*

When over-production becomes imminent we have

the least, because in the Machine Age the predominant consuming power for consumers' goods is in the hands of wage and salary earners. With the evils of foreign investing eliminated there can be no prosperity for capital in the production of services or the production of consumers' and capital goods without prosperity for the wage and salary earners. Prosperity for the heavy industries is dependent upon prosperity for the consumer's goods industries which in turn is dependent upon prosperity for the wage and salary earners.

the condition in the operation of free competition which if allowed to continue will destroy prosperity. It is then that in the best interests of all, the Government should step in and *perform a simple duty* by decreeing that the pay of every wage and salary earner throughout the country be increased by a small flat percentage.

A Currency Unit of Constant Purchasing Power.

There is another very important effect of Government control over the general wage and salary level —control over the buying power of its currency. We hear much about the desirability of a currency unit of constant purchasing power and the control of the general price level. We have had abundant proof in the past few years of the futility of trying to control prices by the volume of bank credit outstanding.

A plentiful supply of money does not necessarily raise prices when consuming power is out of step with productive power.

We are suffering from under-consumption and low prices not because of a shortage of money, but because vast sums are in the hands of savers who are unable to employ their funds in pursuits which would put more money into the hands of spenders. The present glut of unemployed funds is available in the main only for investment in capital goods and financing the distribution of consumers' goods. There is very little incentive for investing in capital goods which would bring more consumers' goods into the market later, while a prospect of greater demand for consumers' goods is lacking.

The amount prices can be lowered by a shortage of money is limited. A contraction of currency and bank credit causes depression and unemployment. Before the War *unemployment caused hunger, and the fear of hunger caused acceptance of lower wages*, thus reducing the costs of production and lowering prices.

With the advent of collective bargaining in determining the wage level, and with the advent of the dole, which removes the fear of hunger, a high bank rate, as a means of lowering prices, lost much of its potency. Great Britain was forced off the gold standard in 1931 because deflationary measures were no longer successful in forcing down wages and prices to a level that would enable British goods to move freely enough into foreign markets and thus replenish Britain's gold reserves. The degree to which wages and prices in Great Britain can be lowered through a contraction of currency and bank credit is limited.

A Change in Wages Changes Prices.

Certain European countries, labouring under the delusion that they should lower their internal price levels instead of lowering the exchange rates of their currency units, have recognized the limitations of bank credit restriction as a means of lowering prices, and they have decreed flat percentage reductions in their wage and salary rates.

Under free competition, prices are governed by the costs of production, and the costs of production are mainly labour costs and capital costs, but to-day's

capital costs result largely from labour costs yesterday. Just as labour is the foundation of all wealth, wages are the foundation of all values. Other conditions being equal, a rise in wages and salaries would raise prices, and likewise a reduction would lower prices.

The control of the price level, or the control of the buying power of the currency unit, is possible by no means except by control over the general wage and salary level. Only by that means can prices be moved up or down at will. *Control over the buying power of its currency unit is a Government responsibility.* The Government should be afforded the only possible means by which it can discharge that responsibility.

We have observed that when prosperity is ruling it is essential that the general price level be prevented from falling. After higher prices and prosperity have been restored the provision of a currency unit of constant purchasing power—a steady general price level—by the only possible means *is the simple service we should ask the Government to perform* in order to preserve a balance between the power to consume and the power to produce under free competition.

The development of present-day factory machines would have been impossible without unvarying standards for measuring weight, distance, and time. We can only flounder along while we attempt to measure with a varying yard-stick of value the many factors involved in the smooth operation of the economic machine, the purpose of which is to afford

the maximum satisfaction to all from the utilization of the products of the factory machines.

A Higher Price Level Required for Restoring Prosperity.

A higher general price level is required for restoring prosperity. The Chancellor of the Exchequer and many others have pointed out the need for a higher price level. Nothing brings about a strong attraction between idle capital and idle labour like rises in prices under free competition.

When prices have fallen below a level which has been maintained for several years, prosperity has not ruled again until the former higher price level has been restored.

Higher prices can be achieved through a greater demand for goods or through higher costs of production. Why not kill two birds with one stone by raising wages and salaries?

As mentioned previously, the Governments of several European countries have decreed reductions in wages and salaries for the purpose of lowering their prices. Naturally they have succeeded in lowering their prices, but in consequence their suffering from the effects of low prices has been intensified. They took exactly the wrong course. Why should not Great Britain take the right course and free herself from depression by the Government decreeing a *rise* in *all* wages and salaries?

At the first thought of raising the general price level in Great Britain by a rise in wages many would say, "That would be all right if all other countries did the same, but how could we, who depend so

much upon overseas trade, raise our price level without serious harm through the loss of foreign trade, and where would employers get the money for higher wages?"

The first question brings us to another flaw in the economy of the past, the delusion that we must have a fixed exchange rate for our currency unit. We used to think that fixed exchange rates were natural and beneficial, whereas for a nation to fix the price of gold in terms of its currency unit in order to give its currency a fixed exchange rate with other gold standard currencies, was *artificial* in the extreme, and the fixed exchange rate and the means resorted to for maintaining it were often harmful in the extreme. As between the means used by Great Britain for many years and protective tariffs, the former were much more harmful. The practical effect of the latter is really only a one-sided departure from the nominal exchange rates.

Why a rise in sterling prices would improve Britain's ability to sell abroad if the pound's exchange rates were *natural* and rationally managed, and the answer to "Where would employers get the money for higher wages?" will be suggested very briefly in what follows.

The Correct Economy for the Machine Age.

In order to visualize the advantages of controlling the general price level by regulating the general wage and salary level, and in order to visualize the procedure in bringing about lasting prosperity in Great Britain without the slightest

need for any agreements with other nations, let us assume that the Government were enabled to make an announcement similar to the following—

1. As *the control of the buying power of the pound is a Government responsibility*, we are availing ourselves of the only natural and direct-acting means. In order to restore prosperity and to ensure equity between debtors and creditors, public and private, we propose to move to a higher general price level. We propose to have higher wages and higher prices following each other until prosperity is restored. Our first decree of a 10 per cent increase in *all* wages and salaries and in the pay of the unemployed throughout the country is to be effective *thirty days from to-day.* We propose to peg the buying power of the pound at the price level which will bring about the comfortable employment of all British labour and capital. We do not anticipate that it will be higher than the 1926 level. Thereafter we will decree small percentage rises in the general wage and salary level whenever there are signs of over-production and that the general price level will fall if matters are allowed to drift. We do not anticipate there will ever be occasion to decree a lower general wage and salary level on account of the general price level having reached a higher point than that agreed upon as the standard, because the natural tendency in industry is always towards higher efficiency and lower costs of production and lower prices. To ensure equity between debtors and creditors, and to avoid the harmful effects of a falling general price level, we want technological improvement to be reflected in a

higher general wage and salary level and a greater volume of profits, not in a lower general price level. After prosperity is restored a steady general price level in wholesale markets is the ideal for which we will strive in determining whether the general wage and salary level should be raised or not.

2. *The best interests of all demand freedom from artificial economic restraints.* Therefore we propose to interfere with supply and demand only in the sense that demand in general shall be kept in balance with supply, but in all other respects we wish the freest possible operation of the law of supply and demand. All agreements regarding prices and restriction of output in the production and merchandising of goods and services are to be cancelled forthwith. No enterprising employer can complain of free competition when all are paying wages and salaries on a scale that will permit what is produced to be consumed.

3. *We want to encourage high standards of living*, as we regard a higher standard of living the requirement for prosperity in the Machine Age. We believe that spending is quite as important as saving, and we do not wish any wage or salary earner to be deterred from the enjoyment of a good standard of living through fear of poverty in his old age. We are taking over as a Government duty the provision of pensions befitting their former rates of pay for all wage and salary earners when they become unfit for employment. We propose to raise the funds for these pensions by a small tax on all pay rolls, as we believe the cost of taking care of unfit

workers is logically a part of the labour costs of production.

4. We propose to let *our credit currency system* function much as it has in recent years. We believe that there should always be enough money and credit available to commerce and industry to permit the full employment of *all the available labour*, and that more than that to an appreciable degree would be harmful to the best interests of all concerned. We propose, therefore, that the full employment of all the available labour, and not the breadth of the credit base or the amount of gold locked away in bank vaults, shall constitute the index to which the volume of bank credit and currency outstanding is to be regulated.

5. As more stable exchange rates can be maintained by having *all exchange transactions cleared through one organization*, and as we consider supervision over exchange a most important Government responsibility, and that the exchange rate of the pound should rest upon its buying power for British goods and services, the Treasury will be responsible for the exchange rate of the pound in Great Britain hereafter. It will take over at current exchange rates all foreign currency in Great Britain, and all exchange transactions with or by individuals of Great Britain must be cleared through the banks which act as the Treasury's agents at the exchange rates set by the Treasury. The exchange rates will be set so as to keep the desirable amount of foreign currency on hand *without the use of any tariffs*. If the foreign currency on hand tends to decrease materially from

too much importing, the exchange rate of the pound will be lowered so as to decrease its buying power for imports, and increase the buying power of the foreigners' money for our exports, thus increasing our exports relative to our imports, and increasing our supply of foreign currency. On the other hand, if the Treasury's supply of foreign currency tends to increase materially from too much exporting, the exchange rate of the pound will be raised so as to bring about less exporting and more importing relatively, and thus reduce the supply of foreign currency on hand.

We are abandoning tariffs because, while tariffs enable us to keep our exports in balance with our imports by making it more difficult for us to buy foreign goods, they do not make it easier for foreigners to buy our goods. We wish to enjoy the great benefit of free trade in being able to exchange goods costing us less to produce for foreign goods which would cost us more to produce.

The exchange rate of the pound has been artificially bolstered up by tariffs. The exchange rate will be lowered to compensate fully for the higher sterling prices and also to compensate for the removal of tariffs. The *natural* exchange rate thus attained will increase our imports, but it will correspondingly increase our exports, the net effect being that goods which Britain is well fitted to produce will move more freely into foreign markets after sterling prices are raised than before.

We anticipate that other countries will quickly see the folly of their low prices and will follow

our example in restoring the price levels in terms of their currencies to equitable levels, after which the exchange rates of the respective currencies should not be very different from what they are to-day.

We are telling the other countries that we believe their economic difficulties will be overcome if they will achieve healthy price levels for themselves and manage the exchange rates of their respective currencies with the view of keeping their exports in balance with their imports without any tariffs. If they will raise their prices as we raise ours, the exchange rates of sterling will not change much. In any event it will be our aim to manage sterling's exchange rates so that our imports will be materially increased, and our exports correspondingly increased, and it is our belief that this policy can operate only to the mutual benefit of all the countries concerned.

After some progress has been made by the several nations acting independently in the rational conduct of their respective exchange transactions and management of their respective price levels, we will propose the organization of an International Clearing Association by which the Treasury of each nation would pay its exporters for the goods exported and its importers would pay it for the goods imported. Then, by slight changes in the respective exchange rates at infrequent intervals, each nation's exports and imports would be kept in approximate balance. This system would accommodate the needs of an industrialized world with such simplicity, and its advantages when understood are so vast, that it is

bound to be the future international exchange mechanism. Its use would facilitate the liquidation of the War debts, and would permit free trade with economic justice to every nation, *thus removing the great obstacle to world peace.*

6. We have *abandoned any thought of returning to the gold standard.* The periodic enforcement of deflation necessary for adherence to it in order to sell in foreign markets was ruinous to the home market, and the pernicious international rivalry for favourable trade balances and gold was a serious source of international friction, and certainly not conducive to world peace.

The Effect of such an Edict.

Now let us examine the results that would follow such a Government edict—

Everyone would quickly realize that raising wages would raise the costs of production and that sterling prices were bound to rise, and those having funds available for spending would try to make their purchases before prices went up. Many of those having savings which they have put by for investment or a rainy day, would change their minds in view of the security afforded them by a Government pension, and would decide to use such savings in providing more comforts for themselves and their dependants. All this would result in an immediate greater demand for consumers' goods.[1]

[1] As a matter of fact, prices would start rising and idle capital and idle labour would start going to work as soon as favourable action on the proposal by Parliament appeared possible, and labour and capital would probably be fairly comfortably employed before the proposal could be enacted into law.

The concerns which have been sheltered by price-fixing and quota arrangements, and have not felt an urge to modernize would find themselves in a highly competitive position. They would quickly realize that they would have to improve their methods in order to stay in business, and would make haste with their improvement programmes. Many people having funds available for investment would try to convert them into capital goods before the depreciation in the buying power of money took place. Capital goods would be in demand at once.

Idle capital and idle labour would go to work!

Where would employers get the money to pay the higher wages and salaries? The answer is simple. The time lag characteristic of economic adjustments would be intelligently utilized, allowing prices to advance sharply before the first decree for a rise in wages became effective. Prices in general would rise faster than wages, and for a time the buying power of the individual's wages would fall, but this would be corrected later on by the rises in wages when the benefits from more efficient methods and volume production tended to lower prices under free competition.

The banks would find no difficulty in accommodating a prosperity that was based upon the restoration and then the maintenance of a former higher general price level; incidentally they would find it very profitable.

The attraction between the idle labour and the idle capital would be irresistible, and if a certain amount of caution were not exercised, there would

quickly be a stress for immigration. Regardless of the density of population *there would be a constant shortage of labour* under an economy which would ensure consumption in balance with productive power. The wants and desires of man are without limit, and as the wants of one can be gratified only through the labour of others, there would be a constant demand for labour, and capital which is only "stored labour," at high wages.

The higher wages were for current labour under free competition the greater would be the demand for "stored labour" to expand production and to provide labour-saving facilities for reducing current labour costs in production. Thus, under an economy which would ensure a constant balance between productive power and consuming power, the advance into higher and higher standards of living for all would proceed without interruption.

Higher efficiency through its tendency to lower prices would result in higher pay and higher buying power to wage and salary earners. Thus the highest possible efficiency on the part of labour as well as capital would be constantly encouraged. *The interests of labour and capital would be rendered mutual.*

The Wage Level which is Best for both Labour and Capital.

After prosperity is restored and all are comfortably employed, labour on the whole could gain nothing honestly from a rise in wages that would raise prices under free competition. To give out claims for

goods and services in excess of the supply of goods and services would cause prices to rise, and profiteering by a few at the expense of the wage and salary earners in the main would be inevitable for a time.

On the other hand, with important leaks through foreign investing stopped, capital would lose if wages and salaries were not paid on a scale that would permit what was produced to be consumed, and that would ensure a firm general price level.

After prosperity is restored *a steady general price level in wholesale markets would afford the index* or the basis upon which labour and capital could always rely for adjusting wages and salaries to a level that would ensure the maximum possible advantage to each.

The Paradox in the Relation between Wages and Profits must be Understood.

If Great Britain is to increase her exports she must increase her consuming power for imports. In the present stage of world industrial development a nation can produce more only if it consumes more. Each nation must depend solely upon its own resources in consuming power for its prosperity.

When all wage and salary earners are fully employed under ever-increasing efficiency and with ever-increasing buying power, the possibilities of the outlet for British goods in the home and foreign markets are staggering.

The standard of living in Great Britain is limited only by her productive power. The profits in sight for capital in bringing about a very high standard of

living through the provision of greater and more efficient productive facilities and through free trade are also staggering.

The paradox in the relation between wages and profits must be understood, or the great advantage to all from private enterprise and the reward of personal efficiency will be lost. Wages are not only the important item in the cost of producing goods, but they represent the consuming power of the masses for the goods produced.

The prospect of higher wages would bring higher prices, but rising prices would stimulate more spending for consumers' goods and more investment in capital goods, and would quickly bring about the full employment of labour and capital. The full employment of labour and capital brings the advantage of higher efficiency through volume production and the use of better methods. Higher efficiency not only permits the opportunity for more profit, but it permits higher pay with higher consuming power for wage and salary earners. Obviously, the consuming power and opportunity for profit are greatest when all are comfortably employed with no unemployed to support, and when there is a wide spread for the tax burden.

Obviously, too, under the latter condition the real value of wages and profits would be enhanced.

The Farm Problem.

The return of industrial workers to the farms will not bring high standards of living.[1] The present farm

[1] More workers would be required on the land under a correct tariff policy as suggested in Chapter IV.

problem will be solved only by a demand in other industries for workers now on the farms. A shortage of workers on the farms, which will permit higher prices for farm products and higher wages and higher standards of living for farm workers through labour-saving methods, is the solution of the farm problem. The solution of the problems of certain depressed industries is along similar lines. They can be prosperous only when the country as a whole is prosperous, and must see the wisdom of raising all wages including their own.

No industry should be at a disadvantage with others through the operation of protective tariffs. Any industry can be healthy and function for the best interests of all only if it stands on its own feet and is independent of artificial props which can be changed according to the whims of the Party in power.

Which Shall We Choose ?

The gold standard, with the value of money varying with the demand for a non-consumable commodity of limited supply, and the resulting booms, and slumps which increase in severity with the increase in the use of machinery, is certainly wrong for the Machine Age.

After prosperity has been ruling, the old policy of lowering wages when prices start to fall and lowering consuming power and causing a further fall in prices is fatal to employment and prosperity in the Machine Age.

There must be a higher general price level. It can

be soundly attained and then maintained by only one means. When that means is adopted the more absolutely supply and demand rules as arbiter in all other economic issues the greater will be the prosperity for all. Shall we continue under a system which causes a constant conflict in the interests of labour and capital, and in which we are hampered by artificial restraint at almost every turn? Shall we continue in confusion and deadlock, and fail to realize the tremendous possibilities of the Machine Age?

Or shall we have a currency unit of constant purchasing power, so that the interests of labour and capital will be rendered mutual, and so that we may enjoy freedom and a natural outlet for our ambitions and our energies, permitting them to be translated freely into accomplishment and a standard of living limited only by our abilities and desires to produce?

We have been making the problem of getting out of depression altogether too complicated because we have been attempting to treat the many involved symptoms instead of the simple cause.

We are in depression because we have failed to recognize the transcendent economic importance of wages in the Machine Age.

Whenever prices have ruled at a certain level for some time, as they did during the War and in the 'twenties, and then fall materially below that level, prosperity cannot be achieved in any reasonable time without restoring the former general price level. Furthermore, whenever a general price level

that permits prosperity is reached, prosperity never lags so long as that price level remains firm under free competition. Therefore, as wages determine prices the simple requirement for lasting prosperity in this country is *wages and salaries always on a scale that will maintain the general price level of* 1928 *firm under free competition.*

While this is a very short statement, it embraces a new economy—an economy wrought not in the short-sighted interests of production, but in its best and long-range interests. It comprises an economy for *consumption* as well as *production.*

The more deeply it is reflected upon the more clearly a strict adherence to it will be seen to be the correct solution of any internal economic maladjustment, and any objections to it from a theoretical or practical standpoint will vanish. Also it will be found that the pre-War orthodox thinking in regard to the determination of wages and the buying power of money, and in regard to international trade and exchange, was shallow and fallacious. Also it will become apparent that each country is solely responsible for its prosperity and that no international agreements are necessary.

CHAPTER II

CURRENCY UNIT OF CONSTANT PURCHASING POWER AND ITS ADVANTAGES

When the consuming power for a country's goods and services is well under its productive power a large volume of idle money has very little, or very slow, effect upon prices. When consuming power is in balance with productive power the position changes, and if more money is then available to commerce and industry than is necessary to accommodate that desirable balance prices rise, and if less is available prices fall.

In this and subsequent chapters it is generally assumed that the money and bank credit available is just sufficient to accommodate the comfortable employment of all the available labour, and that only the yield from industry is available for spending and investing. What happens when the amount of money in use is not in harmony with that condition and how it is to be made to harmonize with that condition are dealt with in Chapter VII. Also the effects of international trade upon prices is largely left for consideration in Chapters VIII and IX.

The credit currency loaned to the banks by the central bank against sound obligations of commerce or of the Government, which is retired as the obligations are liquidated, affords the ideal currency. The ease with which the supply, when unhampered by gold, can be expanded or contracted to suit

the sound demand exactly in each nation, invests credit currency with the possibility of becoming one of the greatest aids to the material well-being of mankind ever invented.

Instead of fettering our bank-notes with gold, and making them cheap when all other useful commodities and property are dear, and dear when all other useful commodities and property are cheap, the purchasing power of our bank-notes should remain constant, corresponding exactly with the average value of all the other useful commodities by which most bank-notes are, or should be secured.

To illustrate briefly, suppose the following list represented the commodities to be used as a basis for regulating the purchasing power of our bank-note currency, each commodity being weighted approximately in proportion to the amount consumed in the nation—

200 lb. sugar, 2,000 lb. flour, 250 lb. beef, 100 lb. pork, 25 lb. cod fish, 50 lb. salt, 50 lb. butter, 15 bushels potatoes, 250 lb. beans, 6 dozen oranges, 6 dozen bananas, one barrel apples, 50 gallons milk, 50 lb. wool, 150 lb. cotton, 25 lb. linen, 10 tons coal, one-half ton pig iron, 50 lb. copper, 25 lb. lead, 10 lb. aluminium, 500 common red bricks, 500 lb. cement, 100 lb. lime, 500 ft. lumber, 1,000 lb. newsprint, 100 lb. rubber.

(As a matter of fact many more standardized manufactured commodities would be used in actual practice, and each would be weighted in the approximate proportion to the quantity consumed by the nation. Mr. Irving Fisher, Professor of Political Economy at Yale University, in his *Stabilizing the Dollar*, shows that, as a basis for the purchasing value of a currency, wholesale prices are more dependable than retail prices, because they are more responsive to changes in the supply and demand. Also, the author would suggest, they are tied closer to the costs of production in most instances.)

Next, let it be assumed that at certain designated commercial centres all these commodities, in the quantities specified, and to definite specifications, were worth for example, £100 in bank-notes, at the time or level we proposed as the basis for the future purchasing power of our bank-note currency. Whenever this list of commodities under the conditions arranged in the beginning could be purchased for £98 in bank-notes, it would be obvious that our bank-notes were dearer than the standard agreed upon, and we would therefore take the necessary step to cheapen them slightly. On the other hand, if this list of commodities under the conditions arranged cost £102 in bank-notes, then it would be apparent that our bank-notes were losing a little of their purchasing power, and that measures should be adopted to prevent a further rise in the general price level and to cause a gradual return to the £100 level.

Slight alterations in the commodities and in the weighting used would be made from time to time by those in control, as changes would be desirable on account of new inventions and changes in the living habits or practices of the people. With the exercise of due care, the purchasing power of a sound bank-note currency could be made practically constant for all time.

In an obligation contracted to-day for liquidation twenty years hence, do we want the same amount of gold then as is involved now, or do we want the same amount of purchasing power then as is involved now?

As suggested previously, the purchasing power of any nation's currency for its own products depends

upon the cost in terms of its currency of producing those products. As the costs of production are mainly direct and indirect labour costs, the purchasing power of an industrialized nation's currency for its own products depends upon the pay of its workers. Other factors being equal, high wages in terms of its currency give its currency low purchasing power for its products, and low wages give the nation's currency high purchasing power for its products.[1]

Assuming that the average wages paid in the U.S. are $24 per week, then, with sterling off the gold standard, if the average wages paid in Great Britain were £24 per week, the purchasing power of £1 would be about the same on the whole as the purchasing power of $1. The effect of wages upon the purchasing power of a credit currency was fully demonstrated during the War.

A little consideration will reveal that there is no other way for maintaining the purchasing power of a sound bank-note currency unit constant in wholesale markets *than by increasing wages and salaries* when wholesale commodity prices tend to decline, *and by preventing further rises in wages and salaries* when wholesale commodity prices tend to rise. *Exactly*

[1] It is commonly stated that supply and demand control prices. Under free competition when the gold standard worked effectively, supply and demand controlled prices because they controlled wages. It happens, however, that competition is not free now, and that supply and demand no longer control wages. With the advent of collective bargaining and the dole, the law of supply and demand has little effect upon wages. If supply and demand controlled wages we would not have millions of able-bodied workers living at a bare subsistence level, while others of no greater skill are enjoying a much higher standard of living. If supply and demand controlled wages, wages would be much lower in the present depression, and prices would be correspondingly lower, and employment would have reached a lower level.

the opposite procedure has been responsible for periods of rising prices and distressing deflation in the past.

There can be no worthwhile prosperity anywhere in the Machine Age while the old idea prevails that the buying power of money, regardless of the variations in its buying power, should determine the wage level.

The idea that the buying power of money should determine wages, regardless of how much that buying power varies, is a hang-over from the days when gold was about the only money in circulation. Naturally under that condition the buying power of gold determined wages and prices. Since that day, however, bank-note currency has been invented and, due to the great advantage to all, banks have been enabled to expand bank credit to accommodate the money needs of modern commerce and industry. Also, since that day industrialization has developed to the extent that the bulk of consuming power is now in the hands of wage and salary earners. It has become plainly evident that the tendency in industry is always towards higher efficiency in production and that therefore the buying power of the workers should be continually rising and never falling, and thus collective bargaining has become an obstacle to lowering wages to accommodate a money the buying power of which varies.

At times the workers, particularly of the U.S., have been practically free from the domination of gold, but at other times, because gold has been tied to their bank money, many have been almost crushed by its domination. This condition of

"half free and half slave" has led to serious confusion and almost disaster at times. If we are to be the slaves of gold we should move back resignedly to the ox-cart age in industry. If we wish to enjoy the advantages possible to all in the Machine Age we must be entirely free.

The time has come when the factors depending upon the buying power of bank credit and bank-note currency are so many and so important to the health of industry that there can be no success while that buying power is allowed to rise and fall. That which soundly determines the buying power of bank credit and bank-note currency must be recognized and utilized to the end that variations are avoided.

The buying power of currency must be fixed at the level which is fair to all concerned by the only possible means—keeping the pay of the workers at the right level.

The Ideal Mechanism for the Regulation of Wages.

Before discussing the very great advantages of a currency unit of constant purchasing power, and the very great advantages to be gained in the present situation by adopting higher price levels, let us consider the ideal method of regulating wages.

(The equitable price level at which the purchasing power of a currency should be stabilized is dealt with in Chapter III.)

We have already become accustomed to allowing a human agency to exercise arbitrary control over the

interest rate for capital's most important instruments, currency and central bank credit, which has very far-reaching consequences upon our well-being. We should, therefore, have no difficulty in accustoming ourselves to allowing the same, or a similar co-operating governmental authority to make decrees regarding the general wage and salary level for the purpose of maintaining a constant purchasing power of our currency unit and bringing about the ideal in industry.

By enabling a governmental authority to make recommendations or decrees regarding the general level of all wages and salaries from time to time, we would have the essential means at our command for maintaining the buying power of our currency unit stable. When wholesale commodity prices were tending to sag below the general level agreed upon as the standard, which would mean that the currency unit was tending to have a higher purchasing power than the level agreed upon, the Government would then decree a small percentage increase in wages and salaries on the understanding that it would apply equitably throughout the nation. Thus the purchasing power of the currency unit would be slightly reduced through higher costs of production and the demand for goods would be brought into step with the supply.

In the same way, if commodity prices were tending to rise above the level agreed upon, the purchasing power of the currency unit should be prevented from falling further, and an opportunity should be afforded for its purchasing power to

appreciate a little. This the Government would accomplish by preventing any rise in the general wage and salary level for a time, and it would thus allow a little more opportunity for the supply of goods to catch up with the demand, with justice to all concerned.

Should the Rises in Wages and Salaries Always be Uniform?

There might be objections to allowing the Government to discriminate between crafts or between the various districts of the country in raising wages. Still, there are reasons why it would be desirable for the central Government to be able to discriminate, and a discussion of those reasons is in order.

In raising wages and salaries to raise prices and achieve prosperity, it could be assumed that the present relative rates of pay of the various crafts and in the various parts of the country are equitable, and that the present rates have resulted from a fairly free operation of the law of supply and demand as it affects the relative rates of pay. For a time it should be assumed that all wages and salaries are too low, and that there is unemployment in every craft and in every part of the country. Therefore the Government should decree rises in wages by small percentages that would apply uniformly to every employee throughout the nation.[1] As time passed, however, some departure from this rule would undoubtedly prove desirable in the best interests of all concerned.

[1] It will be pointed out later that the Government need not have jurisdiction over the higher salary rates.

Questions would naturally arise from time to time as to whether this craft was not being paid too much, or as to whether that craft was not being paid too little. Also, questions would naturally arise as to whether the wage and salary level was not too high in one district of the nation and too low in another district.

If there were a surplus of moulders, for instance, while all other crafts were comfortably employed, it would be obvious that the pay and/or the working conditions of moulders had attracted more workers to that occupation than there was a demand for. This lack of a demand for all the skilled moulders might be due to labour-saving improvements in the process of moulding, or it might be due to the substitution of other products for the products requiring the services of moulders.

Whatever the cause of the surplus moulders, it would be desirable to reduce the number of men training to be moulders, and to divert moulders already trained into other lines in which there was more demand for workers.

Such a situation should be corrected by a reduction in the pay of moulders relative to other crafts. This would reduce the attractiveness of moulding as a trade to beginners, and induce certain moulders to take up other trades. Individuals should always be free to enter any craft. Therefore, in a situation similar to the one assumed when there was a falling tendency in the general price level which called for a rise in the general wage and salary level, it would prove best for all concerned if rises were withheld

from crafts in which there tended to be a supply of workers in excess of the demand.

In a similar way, if there were more unemployment in one part of the country than in other parts, it might be due to wages and/or taxes having been too high in that part. Costs being too high in one part of the country would handicap that part of the country in its competition with other parts, and would tend to reduce the demand for the products of that part of the country. The correction for such a situation would obviously be a reduction in wages as compared with other parts of the country.

Capital for productive enterprises naturally flows to those districts having superior advantages in the supply of raw materials, transportation facilities, power, etc. Other conditions being equal, districts having such advantages can pay higher wages than those less fortunately situated. To some extent living conditions play a part in determining wages, and many are willing to take less pay in order to live in an agreeable climate and pleasant surroundings.

A surplus of workers in one part of the country might be due to too many workers having congregated there because of the more desirable living conditions. The obvious correction would be a little more compensation relatively for the workers in the other parts of the country. By omitting to increase wages and salaries in the district having the oversupply of workers when an increase is decreed for the purpose of keeping the general price level up to the standard, it would tend to bring about equilibrium in employment in three ways: (*a*) workers

would tend to move to the districts paying higher wages; (*b*) the lower wages of the district having the over-supply of workers would tend to reduce the cost of its products, and allow them to move more freely into other markets; and (*c*) the higher wages in the other parts of the nation would increase the buying power for the products of the district having the over-supply of workers.

As the continuous comfortable employment of all the available labour is the primary object of a currency unit of constant purchasing power, it would seem that in decreeing changes in the general wage and salary level for the purpose of preserving a constant purchasing power of the currency unit, the Government should keep the primary object in mind, and make its attainment as smooth and as nearly automatic as possible.

The Government should be well informed as to the tendencies toward unemployment in the various parts of the country and in the various crafts, and in the best interests of all the Government should be empowered to assist the free and orderly operation of the law of supply and demand, wherever such assistance would overcome tendencies toward unemployment.

Whenever it was clear that equilibrium in employment as between the various crafts and as between the various parts of the country could be improved by the Government withholding rises in the pay of the workers in certain cases, it should be authorized to do so. Equilibrium between consuming power and productive power with full employment for capital

and labour can be maintained only by operation in close harmony with the law of supply and demand. When we have a currency unit of constant purchasing power, any question as to whether any change should be made in the relative pay of certain crafts or of certain districts of the country could, in general, best be answered by a careful consideration of the special circumstances in the light of the operation of the law of supply and demand as it should affect wages and employment.

Employers and Employees not Competent to determine Correct Wages—"Dispute" Method Wrong.

Just as the law of supply and demand should govern the wages of "stored labour"—capital—for the best interests of all, supply and demand should also be the basis for governing the RELATIVE wages of various crafts of current labour.

Under an economy in which wages and salaries were always paid on a scale that would in general keep the demand for goods in step with the supply, a demand for labour in balance with the supply would automatically follow, and no fair-minded worker would object to having his pay, or the pay of his craft, adjusted relative to the pay of other workers in harmony with the law of supply and demand as it should affect the *relative* wages of the various crafts.

In every case there is a wage which is correct from the standpoint of a steady general price level and a balance between the productive power and consuming power of the nation, and correct from the standpoint of supply and demand as it should

affect employers and employees. Therefore *in each case there is a wage which is correct from the standpoint of the best interests of all.* But to determine that "correct" wage we must have a method more in keeping with our scientific attainments in other lines than the old way of determining wages by a "dispute" between employer and workman, as Adam Smith expressed it.

While supply and demand should be the final arbiter in the determination of the "correct" relative allocations of wages to the various crafts, the operation of the law of supply and demand as it affects wages is now thwarted by many artificial restraints in which the human factor is involved, and its operation is slow and haphazard, whereas for the best interests of all the operation of the law of supply and demand in this respect should be allowed to operate freely and in an orderly way.

We must come to realize that the determination of the "correct" wage requires the consideration of factors,[1] the facts regarding which are not ordinarily available to an employer and his employees, and that if they were, the employer and his employees are not competent to consider those facts and reach unbiased decisions consistent with them. Although the interests of employers and employees are mutual on the whole, we foster ill-feeling between the individual employer and his employees by allowing the wages he pays to be determined by the "dispute" method. While we fail to provide a more business-like method of adjusting wages, industrial peace is impossible.

[1] Some of the factors involved are listed on page 84.

If the liberty of the individual means the right of an employer to let the wages he pays be determined by his ability to bargain in disputes with his employees and *vice versa* regardless of the effect upon the welfare of others, then, in the best interests of all, it is a liberty which must be curbed.

The restriction of the rights of the individual was a favourite argument used against the enactments which fix minimum wages and maximum hours in certain industries. Yet, to-day, there is not an employer in Great Britain who would think of suggesting a repeal of those acts. For the Government to become arbiter in all *important* wage adjustments would be only a logical step further than it already goes in questions affecting wages and hours of work. The economic effect would be similar, but the additional mutual advantages gained by employer and employees would be revolutionary in comparison.

Success is Impossible under the "Dispute" Method of Adjusting Wages—A Wages Board Required.

If we are to enjoy the tremendous advantages possible to all in the Machine Age, we must become accustomed to the authority of a "Wages Board."

This will be a shock to many, and those who have difficulty in reconciling the practicability of a Government Wages Board are asked to consider carefully the vital need for wages and salaries being at the correct level to preserve equilibrium between consumption and production in the Machine Age.

The further industrialization advances the more vital becomes the need for this equilibrium and the more remote becomes the possibility of attaining it for any length of time under the haphazard wage adjustments which characterize the use of the "dispute method" of adjusting wages.

To trust to luck for the vitally essential balance between consuming power and productive power in the present stage of industrialization is about on a par with wishing for the moon.

By studying carefully the clear-cut considerations worked out in this chapter and the next for governing the actions of the Wages Board, it will be found that there would be little if any opportunity for a misuse of the Board's power. If the authority of the Wages Board could be misused to some extent the harm from such misuse would be nil compared with the very great harm which results from the present primitive method of adjusting wages. Furthermore, employers who cater to the home market have always benefited by general rises in wages, and the same would be true of employers catering to the foreign market under the correct exchange policy.

An employer and his employees are not competent to determine by the "dispute method" even the wages which should be paid for their own best interests, to say nothing of the vital interests of all the other employers and their employees.

The "dispute method" of adjusting wages prevents justice between labour and capital, between employer and employer, and between craft and

craft. If the curse of constant strife about wages is to continue, what is to be the end?

The "dispute method" of adjusting wages is quite as ill-suited to the needs of the Machine Age as the ox-cart, and should have been discarded with it.

The old system of haphazard wage adjustments with a constant conflict of interests and turmoil, which results in idleness of labour and capital, must give way to a system that will permit the maximum possible return to both labour and capital, and thus render their interests mutual.

Only a Wages Board armed with the facts and figures pertaining to the balance between consumption and production, the tendencies in wholesale prices, and the relative demand for labour in the various crafts and in the various districts of the nation, can be trusted with jurisdiction over *the most vital economic factor* in the welfare of all.

There is a wage rate in each case which is best for all concerned, and employers and employees must recognize the tremendous mutual advantages to be gained through allowing a Government agency to consider all the factors involved and to determine that rate in harmony with the law of supply and demand in all major wage adjustments. While supply and demand should determine the *relative* rates of pay of the various grades of workers, the *dominating consideration* in setting their rates should be wages and salaries on a scale that will keep consuming power in step with productive power.

If prosperity is to rule, the old clap-trap about a

"fair wage" or a "living wage" and a "fair return for capital" must cease. We must have wages and salaries on a scale that will keep consumption in step with production. Wages and salaries must be paid on a scale that will stabilize the buying power of the currency unit at an equitable price level under free competition. Capital is entitled to all it can get under that condition, *and only under that condition* can it derive its maximum reward in the present day world.

With proper facilities for collecting the pertinent data, a case for a partial or general rise in wages and salaries would become very apparent to all in a little while, and only mediocre ability would be required for satisfactorily administering the Wages Board.

A steady general price level—a steady buying power of the pound—would become such a clear and logical index to which wages should always be adjusted that the man in the street would soon never question its infallible fairness to all.

The degree of justice and intelligence used by the Government in the exercise of control over the general price level would become so plainly discernible to all that there would never be any opportunity for the misuse of that power.

Wages and salaries must be paid on a scale that will keep consuming power in step with productive power for the best interests of employers as well as the employed. A steady general price level—*a steady buying power of the currency unit—is the infallible index* to which rises in wages should always be made after prosperity is achieved. In the best interests of all, and particularly to avoid the

handicap to the doers in industry, *the benefits of volume production and the use of better methods must be reflected in a higher general wage and salary level, and higher profits, not in a lower general price level,* which signifies that consuming power is falling behind productive power, and if allowed to continue can lead only to depression. The desire for higher and higher incomes and a steady buying power of money is universal.

With the benefits from better efficiency being translated freely into higher wages and salaries, and healthy profits, employees would become almost as zealous for better efficiency as employers, and their interests would be rendered mutual in fact as well as in theory.

For success in the Machine Age, the buying power of the currency unit must be stable. Its buying power must be so regulated that it will always buy, in wholesale markets, the same amount of all the standardized commodities consumed in the country, each being weighted in proportion to the total amount consumed. Its buying power must be regulated to a scientifically constructed index of value. This regulation can be achieved only through the control of the general wage and salary level.

A Wages Board should have control of the wages and salaries, say under £800 per year, paid by all important employers, say those employing twenty people or more. The wage rates paid by the larger employers would soon automatically set the rates which those employing under twenty workers would have to pay.

All employers could be left free to make whatever adjustments they saw fit in the pay of their employees getting over £800 per year. Large employers could also have similar discretion over the pay of say 2 per cent of their lower paid employees in a twelve months' period, and smaller employers could be allowed a higher percentage. Under the chronic shortage of labour which would constantly rule such freedom would result mainly in rises to a few employees.

Any employer or group of employees considering that there were good reasons for requesting a change in wages or working hours would submit the case to the Wages Board. Similarly, any district of the nation thinking that it had good grounds for a change in its general wage and salary level relative to that in other parts of the nation would submit its case to the Wages Board.

The employee should be free to bargain with his employer regarding his rate of pay, and the employer should be privileged to use his discretion regarding the pay of individual employees, providing his average rate of pay for those employed was not materially changed.

Because of man's innate desire for a higher and higher standard of living, there would always be a shortage of workers to satisfy the demand under an economy which ensured balance between consuming power and productive power under free competition. The most common routine work of the wages board would be the consideration of applications made by the more efficient employers for permission to

raise their wage rates in order to hold or increase the number of their employed.

To allow employers to outbid each other for labour would cause prices to rise, and would permit certain crafts to profiteer, and certain industries to profiteer more, all at the expense of the many. This condition would stimulate over-investment in capital goods and bring about over-production. Then the over-developed industries would have to take smaller profits during the readjustment of the balance between consuming power and productive power. The maintenance of a steady general price level through the only possible means would protect the best interests of all.

As higher wages and salaries would be required for correcting the effects of a little too much saving, and not enough spending, salaries above, say £800 per year need not be raised with the other wages and salaries by the Wages Board, at least for some time to come. Statistics on the use made of incomes in the U.S. reveal that the greater part of the total saving by salary earners results from the savings of those drawing over of £800 per year. Furthermore, under prosperity salary earners in the upper brackets can always rely upon the law of supply and demand for fair compensation. In prosperity the services of those who have special skill and can plan and direct others are in high demand.

Local Wages Boards.

In a country like the U.S. there should be a National Wages Board, and in each State local

Wages Boards co-operating with the central body to consider all proposals for changes in wage rates. Probably the local boards should be allowed to make changes within certain limits on their own responsibility. The authority of the National Board, it may be argued, would infringe state rights. But the control of the buying power of the dollar, and the balance between the power to consume and the power to produce, is a national responsibility, and if it is to be properly performed the central Government must have control over the factors which determine the buying power of its currency unit throughout the area using it.

If the people of any country are ever right in thinking that for the best interests of all concerned their country is too large to allow the central Government to have final discretion over all the factors which determine the buying power of its currency unit and the balance between the consuming power and productive power of the country as a whole, then that country is too large for one central Government and one currency system in the Machine Age.

To maintain a steady general price level with the object of maintaining a balance between consuming power and productive power through the Government control of the general wage and salary level, the Government should set up a National Wages Board, which would have jurisdiction over all questions relating to changes in the relative rates of pay of the various crafts, and in the various parts of the nation.

The National Wages Board should be constantly

informed regarding the supply of and demand for the various kinds of labour in the various districts of the nation, so that when adjustments of wages were required to maintain the general price level steady, the national board could make allocations to the crafts and districts in harmony with the law of supply and demand.

The Wages Boards would undoubtedly find their duties more arduous in the first few years of operation under a currency unit of constant purchasing power. But the understanding that their decisions must be in harmony with the law of supply and demand should enable them to render decisions that would be satisfactory to those concerned. After a time, troubles arising from the demands for unsoundly high wages by certain crafts would be ironed out, and what was fair and in harmony with the best interests of all would readily become discernible to all.

The various crafts would soon realize that one group could not gain from a higher relative rate of pay without tending to lower the rates received by other groups. Also they would often find that the opposition to a group seeking higher pay would come mainly from other groups rather than from the employers of the group seeking higher pay. In competitive industries, employers would not be greatly concerned by a higher wage scale in their industry as long as all employers of the industry had to make the same wage adjustment and as long as the rise in prices required, if any, to compensate for the increased labour cost did not tend noticeably to decrease the demand for their products. From their

study of the effects of higher wages, many authorities claim that a rise in wages does not necessarily increase the costs of production, within certain limits.

If a group of workers struck for a higher rate of pay when the supply of and demand for workers in their group did not justify a higher rate, public opinion would soon become educated, and fail to support strikes for rates of pay not justified by sound economic considerations.

When operating under a currency unit of constant purchasing power which would ensure higher wages as better efficiency tended to lower prices, all workers would soon realize that for higher pay, higher efficiency must be attained. Each craft would soon become zealous to see that its members were practising high efficiency and would be quick to point out wherein workers of other crafts were not doing likewise.

With economic justice being administered by the Wages Boards, economic losses and bad feeling resulting from strikes would soon become only memories of the crude and haphazard system of the past.

With the interests of labour and capital rendered mutual, the closest possible co-operation between employees and employers for higher and higher efficiency would be constantly encouraged.

In the U.S., to set up the machinery for soundly controlling the purchasing power of bank-note currency, and enforcing it legally, a constitutional amendment might possibly be required, which would

entail delay. It is believed, however, that a plan could be quickly worked out for restoring prosperity and equity in industry, *so eminently fair to all concerned* and so simple that it could immediately become 100 *per cent effective*, merely by recommendations regarding the general wage level by the Government, which would be gladly and faithfully followed *voluntarily* by all employers and employees throughout the nation. *For enforcing such recommendations, public opinion would be almost as effective as any law.*

In a democracy, the responsibility for the control of the purchasing power of its currency falls squarely upon the Government. Therefore it would seem that the Government of a democracy could be trusted with authority over the only possible means of regulating the purchasing power of its currency to a constant level, which would be 100 per cent effective for preventing either rising prices or falling prices. While it is desirable that in most of its phases industry should be free from any artificial control, there are certain phases demanding concerted action, and owing to the effects of competition, Government responsibility is necessary if concerted action is to be achieved.

Precision and equity by concerted action in the control of the economic forces involved in changing the wage and salary level, are no more possible without Government assistance than the present eight-hour day would have been possible without Government assistance.

In all the previous depressions it was claimed,

just as now, that there was too much machinery and that man's ability to produce had outrun his ability to consume. In the present depression that view is prevailing to the extent that endless Government boards are being provided to interfere with economic liberty, and to stabilize inefficiency, useless employment and a host of unemployed on doles. An economy is being pursued which will hold the country firmly in depression. Instead of the economy for depression, the economy for prosperity should be pursued. Economic liberty with consuming power in step with productive power should prevail. The endless Government boards having countless indefinite and unsound responsibilities under which we are now doomed, should be replaced by a single comparatively small Government board having very definite and clear-cut responsibilities—adjusting wages, and salaries in the lower brackets, from time to time in harmony with the law of supply and demand for the purpose of stabilizing the buying power of the currency unit at the right level.

The Ideal in Industry.

A little consideration will reveal that by soundly regulating the purchasing power of a sound bank-note currency to a constant level by the only possible sound means—regulating the general wage and salary level—the following very desirable ends would be achieved—

Each improvement in the efficiency of producing goods would tend to make goods cheaper, but with goods tending to become cheaper, wages would

have to be increased to maintain the currency unit at the purchasing level agreed upon. Therefore, each improvement in the efficiency of production would automatically tend to bring higher wages to the workers, thus bringing greater spending power for more goods and ensuring equilibrium between consuming power and productive power.

Under free competition, as new machines or better efficiency displaced workers in one industry, the cost of producing the products of that industry would tend to be reduced. This would tend to lower the general price level of all the commodities to which the purchasing power of the currency unit was regulated. Therefore, the wages of all the workers employed would have to be increased, which would bring greater spending power and more consumption of goods with a demand for more workers in all industries. Workers are now told that this desirable result should come about when they are encouraged to work themselves out of employment through increasing their efficiency, but owing to the operation of the economic forces involved under the haphazard system now prevailing, sometimes there is a demand for more labour in other industries and sometimes there is not.

If an important industry became depressed through an important slump in the demand for its products due to a new invention, or for any other cause, repercussions would be quickly felt in the other industries. The laying off of large numbers of employees in one industry would reduce the buying power for the products of the others and there would

quickly follow a tendency for all prices to weaken. If free competition were allowed or enforced prices in all industries would fall, debtors would be ruined, and unemployment would soon be ruling on a terrible scale. But interfering with free competition is exactly the wrong course to take in such an instance. The consuming power of the country should be kept in balance with the productive power through rises in wages that would maintain the general price level firm under free competition. This would tend to raise labour costs and provide keener competition in the other industries, and also it would provide a demand for more of their products which would be translated into enlargements and improvements and the development of new industries, thus providing employment for the available capital and labour. This procedure would be much better for the other industries than allowing them to languish under a reduced consuming power for their products. Keener competition for a time, resulting from changes in production costs, serves as a very useful tonic to an industry, especially when there is a substantial demand for its products.

Evils from Wages being too High.

As an increase in the consuming power increases the demand for capital as well as for labour, there would always be a chance that, in regulating the purchasing power of the currency unit to a constant level by the only possible means, wages would be pushed higher than they should for the best interests

of all concerned. There would be a desire by capitalists whose wage bills were low compared with their profits, as well as by labour, to have the highest possible wages in order to create the highest possible demand for capital as well as for labour. This would have to be guarded against.

Raising prices above the established level would bring about a shortage of labour and a shortage of capital. A shortage of labour would permit certain crafts to profiteer and would bring a stress for immigration. A shortage of capital would permit certain branches of industry to profiteer. An increase in the demand for goods beyond that which would be accommodated by the comfortable employment of the available labour and the available capital, could be brought about only by increasing wages to certain crafts and increasing the capital costs of production in certain industries, and these extra costs would not be compensated for by benefits from a greater volume of production. If wages were increased beyond the amount necessary to maintain the currency unit at a constant purchasing power, or beyond the amount necessary to maintain the comfortable employment of the available labour and the available capital, profiteering by the few at the expense of the many would be inevitable.

If wages were raised so as to establish a higher price level, the owners of fixed income securities would be injured because the income they received would have a lower buying power for goods. Less of the returns from industry would be required to pay the fixed interest and redemption charges on

capital previously invested. The owners of ordinary shares, and labour, would get what the owners of the fixed interest securities lost. After an agreement was once reached as to the general price level, a rise in prices would benefit the owners of ordinary shares and labour, and would benefit debtors at the expense of creditors. The Government would therefore be unfair to one interest or another if it permitted a change in the general price level from the equitable level agreed upon as the standard. A change from the accepted level would benefit certain interests always at the expense of others, and for any interest to seek a change from the accepted level would constitute dishonesty.

With a currency unit of constant purchasing power, the general wage and salary level would always afford a reliable index of the living standards of the workers.

The Supply of Capital.

As is realized by all, we cannot have high living standards without industrialization, and we cannot have industrialization without capital. In an industrialized nation, labour is helpless without capital, and capital is helpless without labour. It is, therefore, important for the best interests of each that there always be a sufficient supply of the other. Labour's purchasing power is increased by the ability of capital to furnish more efficient machines, and as labour's purchasing power increases, the demand for capital increases for supplying more machines for the production of more goods.

In order to prevent a shortage of capital there

must always be sufficient profits to encourage the saving of sufficient capital.

As in labour's best interest there must always be a sufficient supply of capital to keep it employed and to advance the efficiency of production, labour will do best to be content with a stable commodity price level which will give it comfortable employment continuously and all of the fruits of industry in excess of the amount necessary to replace the capital consumed in industry and to encourage the saving of the desirable amount of new capital.

Likewise in the best interests of the owners of capital there must always be sufficient consuming power to keep capital employed. As the reward to capital depends upon the supply of and demand for capital, capitalists (excluding speculators) would do best on the whole by being content with a commodity price level which would ensure the maximum continuous demand for capital. To allow commodity prices to rise for a time and bring about a volume of production in excess of the ruling power to consume, could only bring harm to capital later.

In society some are born savers, while others are born spenders; each is necessary to the other; both are found in all walks of life, and it makes no difference to the success of industry in which walk they happen to exist. As industry is now financed, the savings of the workers are quite as available to the needs of industry as the savings of the so-called capitalist class.

So far as the health of industry is concerned, it makes little difference whether savings are employed

in industry directly by the savers, or deposited in the banks where they are made available to borrowers for use in industry. The economic machine can remain healthy and maintain full employment for labour and capital only if all its money yield is freely returned. To hoard money is an infinitely worse crime against society economically, than making free use of stolen funds, and hoarding cannot be too strongly condemned.

As industrialization advances, the pay of the workers will be higher, and ownership of small businesses or industries will be less attractive. With stability in industry workers will be able to find ample profitable outlets for their savings in the shares of industrial and commercial enterprises, and their confidence in such investments will increase. With stabilized prosperity, the investments of the workers in the industries in which they are employed will also become a factor in the efficiency of production, as they should.

By agreeing upon the equitable purchasing level of our currency unit, and by agreeing to use the only sound means possible for maintaining that level, we would automatically preserve that balance between the spending and saving throughout the nation as a whole which would enable all labour and all capital to be constantly employed. Automatically, we would have the highest possible wages and salaries for all employees compatible with earnings on capital that would induce sufficient savings for investment in needed new facilities of production. *Automatically, our aspiration—equity in the distribution of the fruits of industry between*

capital and the workers—would be thrust upon us and automatically maintained.

Shorter Working Time?

If it so happened that the efficiency in the production of goods advanced faster than the desire to consume goods, increasing the pay of the workers would not be the complete remedy for over-production. The additional requirement for this condition would be more leisure to the workers for spending, and/or higher taxes for more public works and more social services. It is the author's belief that we in the more developed nations have some distance to go before many breadwinners will be able to produce more in forty-four working hours per week than they and their families care to consume. If some workers are satisfied with less, then they should take longer vacations rather than work fewer hours per week while they are employed, because the latter course would be unjust to those having greater demands for consuming power. Also, shorter working time would mean more idle time to the capital invested, in many industries, and would increase the capital costs in the production of goods.

The Orthodox Theory of Money for the Control of Prices.

The Quantity Theory of Money for "managing" commodity prices might work satisfactorily in a country where no wages were paid and all workers took their remuneration by sharing in the profits made in the goods or services which they produced.

But where the interests of labour and capital are allowed to conflict with each other, its use is very harmful.

Increasing trade increases the need for currency and credit. Restricting the volume of currency and credit outstanding decreases the volume of trade and lowers commodity prices, but freeing currency and credit from restrictions does not increase trade and raise commodity prices when consuming power is out of step with productive power.

A low rediscount rate, after a high rate has been prevailing, *releases the currency and credit brake on trade*, but *it does not* necessarily *stop the slowing-down action of the deflation* which has been in progress, *nor does it open the throttle which turns on more spending*,—the requisite for increasing the momentum of trade.

If, in the best interests of a nation, a change in the purchasing power of its currency unit is required, why should not the Government use the direct and only sound means, out in the open, so that all could comprehend the end desired, its justice and the method of attaining it?

If a higher purchasing power—a lower price level—is wanted—*but it should never be wanted*—then decreeing a small percentage reduction in wages and salaries would accomplish the end desired directly, and would save all the conflict and suffering in bringing about the end desired by the indirect and obscure action of a high rediscount rate.

If a lower purchasing power—a higher price level—is desirable then decreeing a rise in wages and salaries

would get what is wanted exactly and the Government would be spared reproach on account of its utter helplessness to attain the end desired.

The momentum of commerce and industry in an industrialized nation is influenced by the trend in the purchasing power of its currency unit. The control of this must rest with the Government. For such responsibility, *should the Government be limited to the use of the rediscount interest rate—a one-way indirect-acting emergency brake?*

There has been a deep-seated belief in the quantity theory of money for controlling prices. Freedom for the expansion of bank credit permitted the industrial activities necessary to the prosecution of the War, and is an essential to achieving and maintaining prosperity.

Raising the central bank rediscount rate and contracting the volume of currency and central bank credit outstanding in order to lower prices, can stampede debtors into sacrificing the prices of goods in order to liquidate their debts, but that method can be successfully used to lower prices to any great extent only if the workers will accept lower wages. In the many decades preceding the War, Great Britain was successful in maintaining the gold standard, but with periods of very serious unemployment and suffering, through the power of the Bank of England to control the volume of bank credit outstanding and thus to keep British prices sufficiently low to ensure a favourable balance in trade.

With the inauguration of the dole, however,

unemployment no longer compelled British workers to accept lower wages or starve. For that fundamental reason the Bank was unable to force the British price level down sufficiently through deflation as in former times, and was forced off the gold standard in 1931. The strength of the labour unions and Federal relief for the unemployed similarly interferes with the power of the Federal Reserve Banks to reduce prices by the *hunger* method, and in an enlightened age the policy of deflation will never be pursued.

The general wage and salary level determines the general price level. The buying power of the currency unit can be held stable at any desired level only through the control of the general wage and salary level. To attempt to control it in any other way is on a par with trying to make the tail wag the dog.

There need be no fear of the banks not being able always to accommodate the sound needs of commerce and industry with currency and bank credit when the Government relieves the banks of responsibility over the buying power and the exchange rates of the currency unit.

We have had ample proof that there is very little in the quantity theory of money for the control of prices. As Sir Henry Strakosch pointed out, in his Essay in the supplement to *The Economist* of 5th January, 1935, there is a limit to which prices can be reduced by deflationary monetary measures in the present age, and "below which incomes cannot be reduced without provoking the most dangerous kind of social and political reaction."

On the other hand little can be gained by any seemingly sound inflationary monetary measures. To inject more money into the system through the purchase of securities by the banks[1] only adds to the glut of funds already in the hands of savers, which are available in the main for investment in capital goods, or should be, in the best interests of all concerned.

The demand for investments in capital goods is low because the demand for consumers' goods is low, and *prosperity is impossible while there is a shortage in the demand for consumers' goods.*

In allowing the purchasing power of our currency unit to regulate wages, we allow the tail to wag the dog. When we allow wages to regulate the purchasing power of our currency unit, trade cycles will vanish, workers will cease to function economically as commodities, and an over-supply of willing workers would become just as impossible as an over-supply of willing buyers. Then, the people of any industrialized nation would never need to worry about over-population reducing their opportunity for success, as long as the world as a whole afforded sufficient food and sufficient fuel for all.

[1] The banks' purchases of government securities in Great Britain have resulted in a vast store of funds being employed in building, but with so much unemployment ruling the labour organizations have made little headway in raising wages, the fundamental requirement for raising prices and achieving prosperity in the present situation. The labour organizations have also been handicapped in raising prices through higher wages because of the orthodox belief that high wages would reduce British exports instead of greatly increasing them.

To attempt to achieve prosperity through the banks' purchases of government securities, and without raising wages, the purchases will have to continue or there will be a falling off in the demand for labour in the building trades, and at best it can prove only an emergency effort. More is said about the purchase of government securities by banks in Chapter VII and about a rational exchange policy in Chapters VIII and IX.

CHAPTER III

HIGHER PRICE LEVELS AND PROSPERITY[1]

The Vicious Circle

When someone stops buying—someone stops selling.
When someone stops selling—someone stops making.
When someone stops making—someone stops working.
When someone stops working—someone stops earning.
When someone stops earning—someone stops buying.

World's Press News.

On account of the very deep-seated belief that a rise in the prices of a nation's products will hinder the sale of its products abroad, it seems advisable, at the outset of this chapter, to emphasize the point that the prices of a nation's products can be raised in terms of its currency without increasing the prices of its products in terms of other currencies in the slightest degree, providing intelligence is exercised in controlling the exchange rate of the nation's currency. To have artificially fixed exchange rates of its currency with other currencies is a most serious handicap to the continuous well-being of every nation in the Machine Age. Of all the orthodox economic views which are holding the World in depression, and causing international friction, the idea that exchange rates should be fixed is the most damaging. (The rational international exchange policy is dealt with in Chapters VIII and IX.)

[1] Readers of this chapter are reminded of the second paragraph in Chapter II.

Balance Between Consuming Power and FULL Productive Power.

The goods produced in industry have been represented as going into a pool. Capital and labour are paid in receipts or claims (money or bank credit) for the goods and services they put into the pool, and their receipts or claims are given in exchange for the goods and services they take out. Everything goes well as long as sufficient receipts are offered for taking out of the pool all the goods put in, regardless of how great the amount put in may be.

Most of the receipts for putting goods and services into the pool are spent in taking consumers' goods and services out of the pool, that is, they are spent on such things as food, clothing, household comforts, amusements, travel, etc. Other receipts for goods and services put into the pool are saved and invested in capital goods, that is, savings are invested in machinery, plant extensions, new buildings, transportation, and other facilities for the production of more goods or services, and for attaining higher efficiency in the production and distribution of goods and services.

Investment in capital goods results in more consumers' goods being put into the pool later. If too many of the receipts for goods put into the pool are saved and invested in capital goods, the quantity of consumers' goods coming into the pool will exceed the receipts available for taking consumers' goods out. Saving and investing in productive enterprises to the extent that more goods are produced than the consuming masses have buying power for must

result in over-production, unemployment and falling prices under free competition.

Falling prices create apprehension about the future. Fear of more unemployment, lower incomes and business losses, and the possibility of better bargains later, all tend to reduce spending. Receipts for goods put into the pool are not freely used for taking goods out of the pool: hence unused receipts accumulate, less goods are put into the pool, and naturally unemployment for labour and capital increases, causing a vicious circle of less spending and less employment.

When such a situation arises, a change in the distribution of the receipts so that a little more will fall into the hands of the consumers of consumers' goods is the only logical remedy. Higher wages and salaries are required for the consuming masses, which would not only increase the receipts available for taking consumers' goods out of the pool, but would increase the cost of the goods put into the pool. Both effects would operate to raise or restore prices, and thus restore confidence and stimulate the use of the greater amount of receipts from higher wages, and the use of the accumulated receipts, for taking goods out of the pool. This increased demand for goods would increase the goods entering the pool, and therefore increase employment for capital as well as labour.

Whenever there is unemployment, as now, the remedy is to raise prices through the assurance that wages will be raised a little at a time until all labour and capital become comfortably employed. The end sought would soon be achieved, and would

be maintained by raising wages and salaries whenever prices tended to fall below the level which brought about the comfortable employment of labour and capital.

Whenever the spending for consumers' goods falls below the amount required for the consumption of the goods available, unemployment for labour and capital is the inevitable result.

Whenever under the economy of the past we have had over-production and falling prices, it has seemed natural to lower wages, yet this reduces the buying power for goods and reduces the cost of producing goods and starts a vicious circle of falling wages and falling prices.

Falling prices should be the signal for raising wages and salaries, not lowering them!

We are in depression because we have failed to recognize the supreme importance of wages in the Machine Age. Just as labour is the foundation of all wealth, wages are the foundation of all values. Other conditions being equal, a rise in wages raises prices and a fall in wages lowers prices. *The buying power of the pound depends upon the general wage and salary level in terms of sterling.*

Directly and indirectly, wages and salaries are the most important factor in the costs of production, also they are the most important factor in the buying power for the goods produced. If wages are not high enough, consuming power falls behind productive power and prices fall.

If consumption is to be kept in step with production to the great advantage of capital as well as

labour, wages and salaries—the consuming power of the consuming masses—must be raised, whenever the *existing claimants* of the returns from industry fail to utilize its products sufficiently to prevent a recession in the general price level under free competition. For employers to lower wages and lower consuming power for each other's goods when consumption falls behind production and prices decline, is exactly the wrong procedure for success in the Machine Age.

When over-production and falling prices become imminent the remedy is more spending for consumers' goods and/or less saving for investment in producers' goods. Higher wages and salaries would provide greater buying power for consumers' goods, and would increase the costs of production. Both effects would operate to harden prices and preserve equilibrium between consuming power and productive power. Employment for capital and labour would be maintained, and thus the best interests of both would be safeguarded. Capital might have to be satisfied with slightly lower profits for a time, thus reducing the savings available for investment in producers' goods, but slightly lower profits for a time would be preferable to serious unemployment of capital for a longer time. The lower profits for a time, and the higher wages, would be merely the correction of the unhealthy relation between profits and wages, which had been ruling previously.

The paradox in the relation between wages and profits must be understood. The higher wages are, the greater is the demand for capital for saving

labour and bringing about higher efficiency in production. Higher efficiency not only permits the opportunity for more profit, but it permits higher pay with higher consuming power for wage and salary earners under steady prices. The higher the consuming power, the greater is the opportunity for profit.

The economic forces involved in a change of the general wage and salary level are tremendous, and the instant the Government of any nation commences seriously to consider the control of those forces with a little precision by Government decrees, as the means to restore and maintain its prosperity, commodity prices in terms of its currency would start to harden, and before any change in the wage and salary level could take place, a prosperity for that nation, which could be maintained, would be on its way.

Major Douglas has contended that "the incomes acquired by consumers in any given period are less in amount than the cost of the goods produced in the same period." That condition has often, but not always, prevailed.

In the decades preceding the War that condition was often avoided by investing abroad the savings accruing to the savers to finance a foreign buying power for the goods produced for which there was not buying power at home because wages were too low. In those decades Great Britain produced more than she consumed, but now the incomes on those investments compel Great Britain to consume more than she produces.

During the War, the condition of which Major Douglas complains was also prevented by the Government borrowing savings accruing to the savers, and spending them at home for British goods and services. Thus during the War receipts for goods put in the pool were always available for taking goods out of the pool.

In order that the Government could spend savings during the War, saving was encouraged and spending by individuals was restricted. Now, if Great Britain's productive power is to be matched by a power to consume, spending and the enjoyment of higher standards of living must be encouraged in every sound way.

Major Douglas would have the Government print more receipts and distribute them to the workers and unemployed, but the economic effect of issuing receipts or orders for taking goods out of the pool for which no goods have been put into the pool, would be the same as counterfeiting. It would cause greater demand for goods, and prices would rise and profits would rise.

The increased profits and the knowledge that the buying power of money would decline, would stimulate greater activity in the production of capital goods, and thus increase the disparity between the power to produce and the power to consume. To keep the power to consume in balance with the artificially stimulated increase in the power to produce, distributions of greater and greater amounts of spurious receipts would be required. The scheme of Major Douglas would be nothing less than

inflation, and, as always, any joy-ride by such means would necessarily be of short duration.

Major Douglas is proposing to administer a dangerous opiate for temporarily alleviating a symptom of our trouble rather than to treat the cause.

More consumers' goods come to the pool than can be taken out, because too many receipts have fallen into the hands of savers, and have been invested in capital goods—the distribution has been wrong. More receipts for consumers are required beyond any question, but instead of the Government distributing spurious receipts to the consumers when we suffer from over-production, falling prices, and unemployment, the Government, in the best interests of both labour and capital, should merely improve the distribution of the receipts *by decreeing small percentage increases in pay for the workers* and the unemployed, until prices are restored. This would put the idle capital as well as the idle labour to work again, and keeping prices stable thereafter by advancing wages and salaries whenever prices tended to fall would automatically keep consuming power in step with productive power.

Wages Should be Raised before Prices Decline.

As stated previously, capital and labour are paid by receipts for the goods and services they put into the pool. Under a sound economy, the receipts or claims for goods and services received for goods and services put into the pool must originate from goods or services previously put into the pool, or from promises to put goods or services into the pool.

When, by the full employment of the available capital and labour, a certain rate of production is reached, there can be no reduction in that rate without unemployment of labour and capital.

As the standard of living improves, and as the population increases, the volume of the goods and services put into, and taken out of, the pool must increase. Therefore the volume of goods and services put into, and taken out of, the pool should be constantly increasing, and consequently the volume of receipts or claims in use should be constantly increasing also.

In order that the volume of receipts in use may grow with the improvement in the standard of living, and the growth in population, bank credit, which is founded upon the promises to put goods into the pool, must be allowed to expand freely to accommodate the demand. Also unused receipts should not accumulate. All receipts obtained for putting goods and services into the pool should be used freely for taking goods and services out of the pool.

As explained previously, falling prices are an obstacle in the way of free use being made of receipts for taking goods and services from the pool.

Falling prices result from over-production. Over-production results from the investment of too many receipts or claims in capital goods.

When capital and labour are comfortably employed, too much investment in capital goods may be brought about in two ways—

Firstly, the tendency in industry is always towards better efficiency and lower costs of production in

terms of the labour involved. Lower costs of production tend to increase the amount of profits available for reinvestment in capital goods, and tend to lower prices. Any tendency towards lower prices should be offset by increases in wages and salaries, so as to increase the costs of production, and to provide greater consuming power for the increased production. Raising wages and salaries when prices tend to fall would restore prices and restore equilibrium between the consuming power and the productive power.

Secondly, rising prices stimulate borrowing, and investment in capital goods, and thus bring danger of over-production later. With the bulk of consuming power resting with the wage and salary earners, as it does under industrialization, rises in prices cannot proceed far unless a corresponding increase is made in the pay of the wage and salary earners. Therefore, when labour and capital are comfortably employed, a rising tendency in prices should be prevented from going far by preventing any rise in the general wage and salary level. Due to the tendency towards better efficiency in production, this would soon cause prices to recede, and thus check the tendency to bring about too much investment in capital goods. *The general price level must be stabilized.*

Before changes in prices take place, there are ample symptoms indicating that they are impending if matters are allowed to drift.

When capital and labour are comfortably employed stocks of unconsumed goods will increase beyond the

normal before prices are lowered. Also production may be curtailed, causing unemployment before prices are lowered. Likewise the stocks of unconsumed goods will probably decrease below the normal before prices are raised. An increase in the stocks of unconsumed goods indicates that too many receipts have been invested in capital goods. Likewise a depletion in stocks of goods below the normal may indicate that not enough receipts have been invested in capital goods, and that an opportunity should be given for the supply of capital to catch up with the demand.

The Government, therefore, in exercising control over the general wage and salary level for the purpose of maintaining a steady general price level and of maintaining consumption in balance with production, should avail itself of the important data bearing upon the health of commerce and industry, with a view to making the changes in the general wage and salary level *in time to avoid changes in the general price level taking place,* as far as practicable.

In general, the Government should impose no restrictions upon individuals in the use they wish to make of their receipts. It should, however, deeply concern itself with knowing, in a general way, what use they are making of their receipts, so that each may continually be afforded an opportunity to derive the maximum income consistent with his desire and ability to produce, and consistent with a balance between consumption and production.

The following may be mentioned as some of

the effects which depend upon the use made by individuals of their receipts, and which the Government should carefully observe—

(*a*) The total outstanding bank credit,[1] because it is a measure of the total receipts in use, and their volume should be constantly increasing, as should many of the other effects, with the improvement in the standard of living and the growth of population.

(*b*) The amount of funds being invested in capital goods.

(*c*) Amount of funds tied up in unconsumed stocks of goods.

(*d*) Bank clearings, savings, the ruling interest rates, exports and imports, etc.

(*e*) The total loans outstanding for financing hire-purchase or future-payment sales.

(*f*) The total loans outstanding for the accommodation of speculators, if any.

(*g*) The amounts of labour employed in the production of consumers' goods and services and the labour employed in the production of capital goods. These amounts should increase as the population increases, and the healthy ratio of these two amounts would become apparent with experience.

(*h*) The amount of unemployment. With correct management this would always be very small.

By making intelligent use of the information to be derived from the study of the effects such as those

[1] As will be observed in Chapter VII, certain responsibilities devolve upon the monetary authority as well as upon the wage authority if equilibrium between consuming power and productive power is to rule.

listed above, the Government could then make a change in the general wage and salary level for maintaining the consuming power in step with the productive power, in time to avoid the operation of economic forces which would cause a change in the general price level.[1]

Over-production, followed by falling prices and unemployment of labour and capital, results from the lack of a proper control over the general wage and salary level for preserving a steady general price level. When such a misfortune is allowed to happen, it can be corrected only by increasing the consuming power, and raising prices. Raising the general wage and salary level is the most direct and most equitable measure for accomplishing both objectives.

The prime object of the Government in scrutinizing the people's use of their incomes should be for the purpose of keeping the power to consume in balance with the power to produce. A steady general price level would be the aim in the practice of that policy, and the steadiness of the general price level would be an indication of the skill exercised by those directing that policy, and would prove a standard by which their stewardship should be judged.

To Let " Costs and Prices Chase Each Other Downwards " is Wrong.

A falling-off in the earnings of the capital invested in industry is a symptom of approaching economic

[1] It would be desirable that the public be kept as fully informed as practicable of the Government's findings regarding the various factors which indicate the uses being made of the national income.

ill-health, and better earnings for the capital invested in industry, under free competition, is an indication of approaching better times.

In many industries a small net profit on each unit of output affords a handsome profit on the capital invested, and therefore the maintenance of a safe margin of profit is sensitive to changes in the volume of production. For some time now many industries have been languishing from the lack of a safe margin of profit, without which prosperity is impossible. The safe margin of profit has not been earned, either because the selling prices of goods and services have been too low, or the volume of production has been too small. If the trouble were due to selling prices being too low, it might seem on first thought that lowering wages would bring about the safe margin of profit so necessary for restoring the prosperity we desire. In former times under somewhat similar conditions, prosperity was gradually brought about to the few at the expense of the many by reducing wages, and selling more abroad.

However, the more developed nations are *now* so equipped for volume production in industry that it is *only the purchasing power of the masses that can bring any degree of prosperity.* Lowering wages cannot increase the purchasing power of the masses, and therefore cannot bring more spending and volume production. Also, there are several other important objections to lowering wages at this time and *surrendering to an era of low price levels,* among which may be mentioned—

(*a*) The burden would fall inequitably upon workers

generally, and would tend to fall more heavily upon those workers less organized than others.

(*b*) By lowering wages in gold value when there is extreme international pressure for gold, each lower wage adjustment would reduce the resistance to still lower commodity prices. With world conditions as they are, it is difficult to tell how much wages might have to be lowered before equilibrium in the demand for commodities and the demand for gold in world markets would be reached.

Mr. Neville Chamberlain, the Chancellor of the Exchequer, has aptly said "an attempt to obtain Equilibrium by further large reductions of costs would be attended by intolerable suffering and holds no hopes of success. . . . An all-round reduction in costs produces further deflationary effects on prices so that *costs and prices chase each other downwards*[1] without ever getting to equilibrium." The trouble is that reducing costs means reducing wages, and reducing wages reduces consuming power.

(*c*) All debtors would be inequitably burdened by the greater quantities of goods required to liquidate their debts than were required at the time their debts were contracted.

(*d*) Vast public indebtedness was incurred when much higher commodity price levels ruled. Equity, therefore, demands that the tax burden should not be increased by returning more in purchasing power to the holders of government obligations than was originally received from them. The tax burden due to heavy internal public indebtedness contracted

[1] Italics are the author's.

under high price levels becomes intolerable when low price levels rule coupled with less production activity over which the tax burden may be spread.

Great Britain, like all other nations at the present time, is in dire need of higher commodity prices. Fortunately, Great Britain is off the gold standard, and if its Treasury would cease playing the gold standard game, Great Britain could free herself from the influence of the declining gold value of commodities, which must persist under the gold standard or in a nation playing the gold standard game, while the international stress for gold lasts. Fortunately, Great Britain can free herself from the misery of deflation without any international conferences or understandings with any other nations whatsoever.

Why Not Let " Costs and Prices Chase Each Other UPWARDS " for a Time?

All agree that higher commodity prices are required in order to cast off depression and bring equity to debtors and taxpayers. We want greater purchasing power for consumers and higher price levels. *Instead of killing the two birds with one stone by the direct method of raising wages and salaries*, we think exactly the same end should be brought about through some roundabout, indirect, obscure method which could not possibly be nearly as effective or equitable to all concerned. "Reflation" can mean only one thing —higher wages and higher commodity prices following each other in a circle. If either gets a start, the other is sure to follow. Under the law of supply of and demand for commodities which should be

unyielding, and, in the present man-made situation, which will be the easier for man to start?

Many would ask "Where would employers get the extra money for paying higher wages?" Also it would be asked "If raising wages would raise prices how would the worker be any better off after wages were raised than before?" There is need for higher profits in many cases as well as a need for more employment and higher wages, and the reasons why the several needs would be equitably and soundly satisfied through letting "wages and prices chase each other *upwards*" for a time are listed as follows—

1. At the present time there is a vast army of officially unemployed and a vaster army of those who desire work or more work, but who are supported, or partly supported, by relatives and others. The combination of full employment for all the unemployed or partly unemployed, and the relief afforded to those who are supporting them would add very materially to the total consuming power.

2. Higher prices would reduce the amount of goods and services required for servicing the public debt and prosperity would widen the spread of its burden.

3. Higher prices would lighten the burden on private debtors—the initiators and doers in commerce and industry.

4. Through volume production and the use of better methods the amount of labour required per unit of production would fall, which would leave room for higher wages and higher profits under steady prices

at a higher level, and with all the benefits mentioned the buying power of wages and profits would be materially increased.

5. With the operation of all the above favourable factors in prospect, and with the assurance that the buying power of the currency unit was going to be reduced to its 1926 level or thereabouts, there would be a rush to invest idle funds in capital goods upon the first hint that the Government was considering such a programme[1]—there would be a strong attraction between idle capital and idle labour immediately—and consumers' goods would be in greater demand also.

6. Prices in general would rise faster than wages and salaries for a time, and employers in general would have no difficulty in finding the extra money for higher wages under a rational banking policy.

7. Later, however, as the benefits of volume production and better methods tended to reduce costs and prices, higher wages and salaries would be required to hold prices up to the new level, and to keep consuming power in step with productive power.

The experience of the U.S. between 1922 and 1929 affords the best corroboration in history of the above statements. The raising of wages from time to time was the great factor in the continuance of that era of balance between productive power and consuming power. With high wages for labour there were high profits for capital. Unfortunately, however, as is

[1] Some of those versed in the international currency speculation game would desire to convert their domestic funds into foreign funds, if possible, while the devaluation of the domestic currency was in progress. This contingency is dealt with in Chapter VIII.

stated elsewhere, wages were not high enough and the dollar was tied to gold. If wages had been higher wholesale prices would not have started declining in 1926, consumption would have kept step with production, and there would have been safe employment at home for savings recklessly loaned abroad. If the dollar had been cut loose from gold and allowed its *natural* exchange rates, U.S. prices would have been free from external depressing influences.

Could any enterprising employer complain of wages and salaries always on a scale that would maintain a steady buying power of his currency unit, and that would maintain a balance between the full productive power of his country and its consuming power?

Prices Must be Raised—Debtors the Driving Force in Commerce.

Whenever prices have ruled at a certain level for some time as they did during the War and in the 'twenties, and then fall materially below that level, prosperity cannot be restored in any reasonable time without restoring the former general price level.

Low prices seriously burden debtors, who are the driving force in commerce and industry. Debtors are the planners and directors of the employment for savings. When prices fall, interest and repayment charges on loans and fixed interest securities continue at their face value and thus take a greater percentage toll on the selling prices of goods. This, with the fact that the volume of production often

declines, causes debtors further serious difficulty in servicing their former obligations. They are unable to make use of further savings, and a glut of savings for which there is not profitable employment is the natural result.

It is most important *economically* that prices be raised so that debtors may be relieved from the unsound burden of their former obligations and thus be enabled to fulfil their vitally important function in commerce and industry of giving profitable employment to the accumulated savings.

Restoring the former general price level is the only possible means of achieving prosperity in any reasonable time.

In raising wages to restore higher price levels it is important to consider how far this should be carried, how the several classes of society would be affected, and what would be the best price level, all things considered, to adopt as a basis for the permanent purchasing power of the currency unit. The level, once established, should never be departed from. *Therefore, the level adopted must be equitable so that it will be defended for all time.*

So far as all internal Government debts are concerned, the higher the commodity price level adopted the lighter would be the tax burden for paying the interest and liquidation charges. In the same way, the higher the commodity price level adopted, the lighter would the burden be upon debtors in paying the interest on and in liquidating their indebtedness.

Upon first thought it might appear that the creditor would simply lose what the debtor gained, and that

no important economic advantage would result if equity to debtor and creditor were the only object sought by a higher price level; but there is a most important economic consideration involved. It must be remembered that the depression was caused by too great a share of the return from industry falling into the hands of savers, and that the creditor class comprises the savers who have enormous holdings in debentures, mortgages, bonds, preference shares, etc.

When prices fall more goods are required to service the holdings of the creditor class, and the share of the return from industry falling into the hands of savers is thus further increased, and a growth in the returns yielded by industry for which there is not employment is the inevitable result. Thus the disequilibrium which was the cause of the depression in the first place is further aggravated, and the depression must continue while low prices continue. Therefore to restore a healthy balance between saving and spending, and aside from the other advantages of rising prices, it is particularly important economically that the inequitable and harmful toll on industry taken by creditors when prices are low be corrected by *raising prices*.

The debtor who has had vision and the courage to borrow in order to carry out his plans is the initiator and the doer in commerce and industry who makes the profits to the creditor class possible. Low prices mean distress for him, and prevent him from making use of the accumulations accruing to the creditors.

If low prices are allowed to continue this generation will never enjoy prosperity, and to make use of the correct way to raise prices is a paramount obligation of the Government.

To ensure the balance between productive power and consuming power which will permit employment for everyone who desires it, and the enjoyment of a standard of living in keeping with his ability and desire to produce, transcends almost all other obligations of a Government in the Machine Age.

The Effect of Higher Price Levels upon the Several Classes of Society.

Let us note the effect upon the several classes of society of raising the general price level by raising wages—

Wage and Salary Earners would benefit in their purchasing power from a reduction in the tax burden of the public debt, and the higher the commodity price level was pegged the more they would benefit in this respect. They would also benefit from the reduction in the tax rate to cover the current expenses of the Government through the greater industrial and commercial activity over which the tax burden would be spread. All classes would enjoy this benefit. They would benefit in greater purchasing power for goods through volume production up to the point where all labour and all capital would be comfortably employed.

The Industrial and Commercial Enterprises or Corporations producing goods or services would benefit from volume production and the full

employment of their invested capital. Beyond the comfortable employment of all labour and all the available capital they would derive no permanent benefit.

The Banks should benefit materially through the greater industrial and commercial activity. Their profits are derived from the loans they make, and the greater the industrial and commercial activity, the greater should be the demand for the services which banks render and from which they derive profits. Their worry about possible losses in the liquidation of outstanding long-term loans would cease, and any reduced purchasing power of the currency received in payment of those loans, as long as it is equitable to all concerned, should not bother the banks. In other respects the effect of a higher price level upon the banks and their owners would be about the same as the effects upon the industrial enterprises and their owners.

The Private Owners of Long-term Obligations would lose by any reduction in the purchasing power of the currency they would receive at the maturity of the obligations owed them. However, they would be spared the worry about the possibility of default which confronts many holders of such obligations if present conditions do not improve. This applies to Government obligations as well as to private obligations in some countries. Furthermore, many of the present outstanding long-term obligations were contracted at much higher price levels than the present, and equity demands that more should not be returned in purchasing power to the creditor than was originally received by the debtor.

The Bank Depositors would lose by a depreciation in the purchasing power of their funds on deposit, unless they promptly invested those funds in commodities or commodity-producing or marketing enterprises or other property during the period of rising prices.

The Rentiers—Owners of Fixed-interest Securities and Pensioners—would lose purchasing power by a rise in commodity prices. They would gain, however, by a reduction in the tax burden. As the purchasing power of currency would be regulated to a constant level in wholesale markets, all consumers would benefit by the smaller "spread" between wholesale and retail prices that would come about with stabilized prosperity through volume turnover, healthier competition, better efficiency, etc. On the whole, commodity prices could be increased a considerable amount before most *rentiers* would lose more than they have inequitably gained during the deflation of the past six years. Granting they might lose even more, would that be any excuse for continuing to handicap the doers in industry by low prices and for continuing the tragedy of unemployment?

The Owners of Property of Every Kind would benefit from a reduction in the tax burden. Also, they would benefit from the fact that in prosperity the capital invested in property receives a higher return.

Government Employees would be in the same position as other wage and salary earners, and the pay of *all* Government employees should be increased along with the salaries and wages of the workers in

industry.[1] The former are spenders nearly 100 per cent.

The Unemployed on the Dole are spenders, 100 per cent, and unless the dole was increased along with the rise in commodity prices, their present low standard of living would be further lowered. Therefore, the dole should be increased immediately by at least the same percentage as the wages and salaries of the employed. It is not the fault of the unemployed that Great Britain has become partially industrialized before developing an economic system which would keep the power to consume always in step with the power to produce, and that the present system has broken down, leaving them with no useful work to perform.

For willing workers in the midst of plenty to be unable to exchange their labour for the goods they require, is the worst of all economic misfortunes. Under the correct economy there would be no able-bodied unemployed who were willing to work.

The Public Service Corporations. In raising wages to raise commodity prices and increase spending, commodity prices in general would readily take care of themselves. However, *the public service corporations*, which have the charges for their services fixed by the Government, must be allowed to live, and in some cases their charges might require revision if they were to have justice. They should be

[1] This paragraph was written before so many were being employed, particularly by the U.S. Government in its unemployment relief programme, and it applies only to those rendering useful services under the correct economy. In general, the pay of all those who can be dispensed with under the correct economy should be reduced and stopped as rapidly as possible.

allowed higher rates in cases where rising wages prevented sufficient profits. The mere announcement that the general wage and salary level would be raised would be so potent in stimulating business that increasing business would keep well in advance of rising wages for some time at least. A higher volume of business would reduce the overhead charges against the costs of production of transport, gas, power, lighting companies, etc.

Forward Contracts. During the 1922–29 era of prosperity in the United States when rises in wages were prevalent, contracts for buildings, plant construction, etc., requiring a number of months to complete, often contained clauses which protected a contractor from a loss through rises in wages during the execution of his contract. As soon as any agitation commences for the achievement of a prosperity which will be lasting through the only possible means, contracts for forward deliveries will contain similar clauses.

When such clauses were not included in contracts involving some months for completion, a spirit of give-and-take prevailed among buyers and sellers to an extent that very few contractors sustained loss through a rise in labour costs during the execution of their contracts.

Over-developed Industries. Under a system of raising wages to achieve and maintain an equitable general price level there would be a tendency to eliminate high-cost producers. This would be particularly noticeable in over-developed industries, but this is the great advantage of the competitive

system because it stimulates rivalry for productive efficiency which is the only means by which a higher standard of living can be achieved.

It is a short-sighted policy, to say the least, to continue a system of low wages and restricted competition which continues the scourge of unemployment, and prevents prosperity for enterprising employers in order to keep alive high-cost producers in the over-developed industries.

Many industries appear to be over-developed now because of the low consuming power.[1] When it becomes apparent that the potential consuming power will be liberated, many of the high-cost producers will have no difficulty in finding the funds for modernising their plants so that they will be in a strong position under prosperity.

The Equitable Price Level.

From a consideration of the foregoing it is evident that almost all would materially benefit from an increase in commodity prices, and that unless commodity prices were pushed up higher than they were some years ago, not many would lose more than they have inequitably gained through the deflation of the past six years. Also, in the best interests of all, it is evident that no one could honestly ask that commodity prices be raised much beyond the level which would bring about the comfortable employment of all labour and all capital.

[1] As will be shown in Chapter VIII, British export industries and shipping now appear to be over-developed largely because of the effects of British duties on imports. Under free trade and the correct exchange policy those industries would quickly take on new life.

In the United States wholesale commodity prices quickly rose 25 per cent in terms of U.S. dollars in the latter part of 1922, after the raising of wages got started. Judging from experiences of the U.S., it would seem that the mere intimation that the Government proposed to restore higher commodity prices by bringing about a higher general wage and salary level, would immediately cause a rise in commodity prices, and before the general wage and salary level could be raised as much as 10 per cent, wholesale commodity prices would rise 25 per cent or more.[1]

The advantages of volume production and volume turnover in trade resulting from the full employment of all labour and all capital, the enthusiastic co-operation of labour with capital for efficiency in production, and the advantages gained from the knowledge that deflation was a scourge of the past, would be tremendous and almost beyond belief.

To keep commodity prices at the new level, wages would soon have to be increased again to compensate for the lower cost of producing goods due to the advantages of volume production and

[1] The threat of the coal miners of Great Britain to strike for higher wages in the winter of 1935 and 1936 caused a rise in coal prices some weeks before the miners received any increase in wages, and is a good example of the way prices would rise in anticipation of rises in wages.

The snag in raising the wages of the coal miners was the position of the coal exporters. Raising the pay of the coal miners only, would have only a small effect upon the sterling general price level, and therefore would not have much effect in lowering the exchange rates of sterling. For this reason higher wages would reduce the profits of the coal exporters unless they charged foreign buyers higher prices in terms of their currencies, which would probably reduce foreign sales. But if all wages in Great Britain were raised the position would have been quite different, as then *the general price level* would have risen and the exchange rates of sterling would have been correspondingly lowered, or should have been, which would have enabled coal exporters to get higher sterling prices for coal without changing the prices paid by foreign buyers in terms of their currencies.

the use of better methods. Raising wages to compensate for lower costs of production would be an important factor in bringing about the better co-operation of labour with capital for still better efficiency in production. But a very important factor in raising wages to keep commodity prices up would be the greater buying power for more goods. Judging by what happened in the U.S. from 1922 to 1929, it is quite possible wages could be increased 100 per cent or more in Great Britain in a few years' time without raising wholesale commodity prices as much as 35 per cent, and at the same time leave ample room for generous profits to capital.

It is suggested that the proper way to bring about prosperity with the maximum amount of equity to all, would be for the Government to decree an increase in all wages and salaries above the present level of, say, 10 per cent, then 5 per cent from time to time until all labour and capital became comfortably employed. In each case the Government would give, say, thirty days' notice in advance of the time the rises were to be effective.[1]

At first the Wages Board would decree rises in all wages, and salaries in the lower brackets, by the same flat percentage until the 1928 general price level was restored or until labour and capital become comfortably employed. Later as volume production and the use of better methods tended to lower

[1] A longer notice of a rise in wages than thirty days could be given, but it is the author's belief that prices would rise quickly regardless of the amount of advance notice given, especially in the beginning, and the workers would quickly become restive, and rightly so, with commodity prices rising rapidly and wages remaining stationary for a period as long as, say, ninety days.

prices, *as they always do under free competition,* the Wages Board would decree rises or withhold rises to each craft or each district of the nation in harmony with the law of supply and demand, allowing rises in cases where there tended to be a shortage of workers and withholding rises in cases where there tended to be a surplus.

No rises in wage rates would be permitted while there was any tendency towards a rise in the general price level established as the standard. A rise in the general price level could not proceed far, and prices in general would soon recede if the general wage and salary level were held stationary under free competition.

Advance notices would always be given for rises in wages, and in raising the general wage and salary level to raise the general price level and bring prosperity, the prospect of greater consuming power and a higher labour cost in many cases, would cause prices to advance sharply before rises in wages would be effected and thus higher profits would accompany higher wages.

The prospect of greater consuming power and higher prices would stimulate employment for labour and capital in the production of more producers' goods.

Higher prices would reduce the unsound burden of private debts incurred under higher price levels, and similarly the burden of the public debt would be reduced and prosperity would widen the spread for the tax burden. Full employment and relief from supporting the officially unemployed, and the many

others who are being supported, or partly supported, by relatives, etc., but who would prefer to be self-supporting and enjoy a much higher consuming power, would add very materially to the total consuming power. Through volume production and the use of better methods, the amount of labour required per unit of production would fall. This would leave room for higher wages and higher profits under steady prices at the higher level. With all the benefits mentioned, the buying power of wages and profits would be materially increased, and the higher consuming power thus attained would be freely translated into full employment for all the available labour and capital under free competition.

When all labour and capital became comfortably employed in Great Britain, sterling's purchasing power would be stabilized at the commodity price level then ruling. Thereafter wages would be raised to hold the purchasing power of sterling for goods consumed in Great Britain at that level. *If care were exercised, the only changes in wages required to keep sterling at a constant purchasing power would be increases to compensate for the greater efficiency in production as it tended to lower the general price level under free competition.*

In the transition from depression to lasting prosperity through the control of the general wage and salary level, the prospect of a higher price level would cause commodity prices to rise faster than wages at first, and hence rising profits would be accruing to capital while the buying power of wages would be declining. Soon, however, the

buying power of wages would start improving, and would then continue to improve as the efficiency in production improved, and would thus constantly tend to improve. The profits to capital would be subject to the supply of and demand for capital. Under high wages and free competition new capital would always be in high demand, and we would become accustomed to much higher interest rates than are ruling now.

Also, the return on invested capital would be in proportion to the risk taken, in general, exactly as now, and ill-conceived and unfortunately placed investments would be lost, marginal producers would make little or no profits, and the fortunately placed and/or skilfully managed investments would make high profits.

Compromise Required between Conflicting Interests —Errors Quite Possible in Beginning.

It is true that it would be necessary for an agreement to be reached between slightly conflicting interests as to the purchasing level at which the currency unit should be stabilized. As things now stand, the increased commodity value of money has benefited a very small group of society at the expense of a very much larger group. Naturally, the latter group feels that it is justified in seeking to restore to commodities the higher money value which has been lost. The creditors, *rentiers*, and owners of money, on the one hand, and the debtors and all the producers and owners of commodities, on the other hand, are all human beings,

not commodities, and are quite capable of recognizing the conflict of their interests. Also, they are quite capable of arriving at a satisfactory compromise now that would render their interests always MUTUAL in the future.

It should not be very difficult for any of us to admit that the purchasing level of our currency unit at which the comfortable employment of all the available labour and capital is brought about, would be an equitable level at which to stabilize its purchasing power. Also, it should not be very difficult for any of us to recognize a condition of "the comfortable employment of all the available labour and capital" when this condition made its appearance.

To those who think the Government need not control the general price level, through control of the general wage and salary level, the answer is that a currency unit of constant purchasing power, and consumption keeping step with production automatically, are possible by no other means! By no other means can the interests of labour and capital be rendered mutual! The haphazard system of the past will suffice no longer. Unless the Government accepts responsibility for this simple and clean-cut service, which it only is perfectly fitted to render, industrialization has reached such a stage that other more complex services will be forced upon the Government which it is totally unfitted to render. The independence of the individual will suffer, freedom in the choice of his way of life will be restricted, and the standard of living of the masses will fall far short of

the possibilities under the correct economy for industrialization.

To say that wage and salary earners would not see the logic of a wage and salary level that would keep the purchasing power of the currency unit constant, is, in the author's belief, an admission on our part that we have failed to grasp the far-reaching benefits to both labour and capital from the use of a currency unit of constant purchasing power. The workers of several nations have already accepted uniform *cuts* in their pay by Government decrees which were *thought* for their best interests, but which were very harmful.

Prosperity Possible only by High Wages.

In the present depression each nation is dependent solely upon the forces within itself to restore its prosperity. How, then, is a nation to restore prosperity except by increasing its own power to consume?

The present stage in industrialization and the desire of each nation to manufacture for itself make it no longer possible for capital to derive its greatest profits by keeping the share of labour—the great consuming power of each nation—as low as possible. Now, capital in the more developed nations can reap its greatest reward only by the highest possible pay to the workers compatible with a balance between the power to consume and the power to produce. There must be sufficient spending to consume the products of industry, otherwise overproduction with unemployment for capital as well as

labour must result. If there has been so much saving and investing in capital goods as to bring over-production, keener competition and reduced profits for capital for a time are inevitable. Under the economy of the past this keener competition must be endured under falling prices, falling wages, lower buying power, and reduced volume of production.

Under the correct economy for industrialization, any tendency towards over-production and falling prices would be met by a government decree to raise wages and salaries, and the keener competition resulting from a tendency towards over-production would be experienced under higher wages, higher buying power, greater volume of production, and a rising tendency in prices—a condition of which no industrialist could justly complain.

Idle hands and idle capital seeking employment are a sad reflection upon the present-day intelligence.

The Purchasing Power of the Currency for Foreign Goods Must be Mastered also.

High sterling wages would give sterling a low exchange rate, and low wages would give it a high exchange rate, but the cost of British goods to foreigners or the amount of British manufactured goods required to purchase the needed or desired goods from abroad would not change in the least, providing sterling's exchange rates were properly mastered.

For preserving equilibrium in industry, it would be important to control sterling's purchasing power in foreign markets as well as in the home market.

How this should be done is outlined in Chapters VIII and IX.

No Danger from Radical Government.

The man in the street realizes that rising prices always stimulate buying and increase trade, while falling prices have the reverse effect. He realizes that rising prices and an assured buying power for the equivalent of all that can be produced would rout depression overnight.

When prosperity has been achieved, the man in the street will realize that the preservation of a stable price level under free competition is the requirement for maintaining prosperity. Also, he will realize that no labourer or capitalist, no spender or saver, and no debtor or creditor could have a just complaint against a stable purchasing power of the currency unit at the right level.

The man in the street would understand that high wages caused high prices, and that low wages caused low prices, and the desirability of preserving a steady general price level would become just as apparent as the desirability of preserving law and order. The decreeing of higher wages by the Government to prevent falling prices would become just as natural to the man in the street as the levying of taxes for the support of the Government.

Keeping the purchasing power of the currency unit at a constant level in wholesale markets is such a clear-cut service and so eminently fair to all, that no Government could make, or would dare make, a serious mistake in performing that service, because

the man in the street would quickly be able to point a finger to any error made by the Government in not keeping the purchasing power of its currency unit at the equitable level adopted as the standard.

There need be no fear from the actions of a radical party. Nothing turns a radical into a conservative like responsibility. No matter how radical a party may be before it has responsibility, when it is elected to take over the reins of government, it immediately sets about with caution to do those things which will keep it in power. After a higher general price level is established, no Government would jeopardise its chances of remaining in office by disturbing the established purchasing power of its currency unit.

When control of the general wage and salary level is utilized for stabilizing the general price level, and when the exchange rate of our currency unit is regulated to keep our exports in correct balance with our imports without any tariffs—when the gold standard humbug is removed from our economy—the man in the street will be able to qualify as an economist, at least for his own purposes.

A price management that will restore and then constantly maintain a higher equitable general price level in wholesale markets, is the greatest need of civilization. It is possible by only one means. Until that means is utilized, in the present state of industrial development, civilization, at the very best, can only flounder in its progress. To afford its people a correct general price level management, by utilizing that means, is a simple obligation which rests solely upon the Government of each nation, and which, in

an industrialized age, transcends almost all other obligations of the Government.

No nation can achieve success for any time in the present stage of industrial development while its general price level is allowed to float about by economic forces which should be, but are not, intelligently controlled. Only a small part of the benefits possible in the Machine Age can be realized while we fail to recognize the importance of a currency unit of constant purchasing power and fail to utilize the only means by which it is possible. If the people of any democracy cannot trust their Government with authority over that means, then they must reconcile themselves to continuing in depression.

CHAPTER IV

GOVERNMENT ASSISTANCE [1]

MANY have said of the author—"while he advocates economic liberty and the free operation of supply and demand and the non-interference of the Government in commerce and industry, he flagrantly violates that doctrine when he advocates that the Government should set the rates for wages, and salaries in the lower brackets, which employers should pay."

Incidentally, do employees or employers enjoy any great amount of freedom in departing from the ruling rates of wages to-day? It is true that employees can stop work and employers can close their works when they are not satisfied with the rates of pay. So they could if the Government set the rates, and economic liberty could not rule if they were prevented from doing so.

When drastic punishment was first proclaimed for those who committed murder and highway robbery, undoubtedly there were complaints that the liberty of the individual was being restricted. Since that day we have come to realize that the widest possible liberty can be enjoyed by all only if we live under a Government that will enforce law and order, and severely punish those who let their own liberties interfere with the liberties of others.

Liberty, a Government Responsibility.

In general, we have come to realize that we can

[1] Readers are again reminded of the second paragraph of Chapter II.

enjoy the widest possible security in the pursuit of liberty if our code of conduct precludes our doing those things which interfere with the liberty of others. In the economic realm, however, we have been slower in working out a code of conduct which is in harmony with the best interests of all.

The desire for economic liberty is inborn, and we have recognized the advantages of personal enterprise and free competition, and have thought that supply and demand and the survival of the fittest should be allowed free rein without Government interference, regardless of circumstances, as long as murder and robbery were not committed with violence.

The fault is not with supply and demand; the fault is with the environment in which supply and demand operates. A better regulator of a country's various industries than supply and demand is impossible. The evil arises from the lack of balance between the consuming power and productive power of the country as a whole.

The trouble has been that we have gone wrong in considering labour as a commodity like other commodities, economically. It is true that "current labour" is, or always should be, in competition with "stored labour"—capital, but this is only a part of the picture. The great difference economically between the so-called commodity, labour, and the other commodities is that labour has the bulk of consuming power.

If economic liberty is to rule, the prices of the other commodities must be governed by supply and demand, and also wages must be paid in harmony

with the law of supply and demand. It is of paramount importance, however, that equilibrium should rule between consuming power and productive power. If consuming power falls out of step with productive power, the free operation of supply and demand in setting prices and wages would start a vicious circle that would soon bring a complete collapse in prices and employment and *render economic liberty meaningless.*

Therefore, if supply and demand is to govern prices and wages and thus ensure the rule of economic liberty, it is of first importance that consuming power be kept in step with productive power, and hence, while supply and demand should determine the relative rates of pay of the various grades of workers, the *dominating consideration* in setting their rates should be *wages and salaries on a scale that will keep consuming power in step with productive power under free competition.*

As an employer and his employees are incompetent to give proper weight to the "dominating consideration," and for other reasons set forth in previous chapters, the "dispute" method of adjusting wages must give way to the Government control of wages.

If a worker is to enjoy economic liberty in the Machine Age, labour must always be in demand. If the worker is not satisfied with the ruling pay for the work he is doing, or if he is not satisfied with his working conditions or with the opportunity which his work offers for his particular qualifications or abilities, then he should be able to find a demand for his services elsewhere at a rate of remuneration in harmony with the law of supply and demand.

The owner of capital should enjoy similar liberty and to the same extent, but neither the worker nor the capitalist can enjoy a demand for his services upon which his economic liberty depends unless consuming power on the whole is kept in step with productive power, and the latter is possible only if prices on the whole, and therefore wages and salaries on the whole, are maintained at the right level.

To allow an employer the liberty of paying wages, and salaries in the lower brackets, out of harmony either way with that "right level" is allowing him a liberty which interferes with the liberty of others, and, therefore, it is a liberty to be withheld. Just as it has been necessary for the Government to assume responsibility in other spheres for preventing the liberty of the individual from interfering with the liberty of others, *so in the setting of wages*, which determines the buying power of the currency unit and the balance between consuming power and productive power, and is the most vital factor in the economic welfare of all, *the Government must assume the responsibility.*

The Government must assume responsibility for the buying power of its currency unit in the home market, using the only possible means, if we are to enjoy economic liberty, and for the best interests of all the Government must assume responsibility for the volume of credit and currency outstanding as explained in Chapter VII, and for the buying power of its currency in foreign markets as pointed out in Chapters VIII and IX; also there are some special

industries in which a certain amount of co-operation on the part of those engaged in them would be beneficial to all. Whenever such co-operation is desirable it could best be done under the sanction of the Government and under a certain amount of Government responsibility and assistance.

Unfair Competition.

Unfair competition is bad for all concerned. It is manifestly unfair for one producer to dump all of his output, particularly in raw material, into the market as soon as it is produced, or before it is produced as often happens, *compelling others* to bear the burden of carrying the stocks necessary for stabilization and of carrying on research for improving the quality or research and advertising for widening the use of a product. *The producers of consequence* of certain of the basic raw products and standardized commodities should be compelled to organize sufficiently under some governmental authority, somewhat as the railroads are under the Inter-State Commerce Commission in the U.S., *so that the producers* ONLY *would carry the necessary stocks, and would bear the burden of their own over-production,* and so that all would bear their equitable share of the cost of such over-production, together with the cost of advertising, research, grading, standardizing, and marketing.

Unconsumed stocks should not, in any circumstances, be allowed to increase beyond a healthy limit. When such limits were approaching, price reduction and curtailment of production would have to be effected, the aim being in the long run to let

price reduction prevent over-production, in accordance with the law of supply and demand. The co-operative organizations suggested could succeed only if they refrained from wasting their energy by trying to thwart the law of the survival of the fittest.

Whenever any artificial restriction in production was put into effect, it would have to be with the understanding that the selling price would be moved progressively downward while such restriction in output remained in effect.

In such co-operative organizations the voting power for the conduct of the organization's price policy, or any curtailment of output policy, should not be in proportion to the amount of the product produced by the various members, but the voting power governing such matters should be in proportion to the profits made in the production of the product by the respective members during the previous year. This would leave all matters affecting the policy for price-fixing and curtailment of output in the hands of the low cost producers, just as it is now in the long run. This would always tend to bring about the free but more orderly operation of the law of the survival of the fittest, which is desirable beyond any question.

It is possible for the best interests of all concerned that the low cost producers should have a greater voting power on price policy than that proposed. Possibly only the producers of the lower-cost-half of the production should be allowed to vote on price and restriction in output policies.

Restriction in output, when advisable, would apply

to all producers alike, and could be pro-rated on the basis of the production of the respective members during the previous year, or on the basis of capacity to produce in the case of new producers.

A product imported from other countries should be marketed through the organization having jurisdiction over such product, and the foreign product should bear its equitable share of the cost of carrying stocks for stabilization and the operating expenses of the organization. In cases where curtailment in production was effected, the importers of the products involved should be placed upon a quota based upon their previous sales, in the same way as domestic producers. With prosperity stabilized, the supply of most products would, as a rule, respond closely to the demand, but such products as cotton and wheat, for instance, would always require close attention on account of the varying parts sunshine and rain play from year to year.

The detail work and the expense required for such stabilization should be borne by the organizations themselves, leaving as little as possible for the Government to perform.

Capital should be free to enter any industry just as any worker should be free to enter any craft for which he is fitted by his taste and capability. The small and inefficient concerns are bound to give way to larger and more efficient concerns as industrialization progresses. In prosperity it often becomes more remunerative to work as an employee of a large efficient concern than as an owner of a small inefficient concern.

Control of Exchange Rates is Better than Tariffs.

The maximum advantage to any nation from being able to exchange goods costing it less to produce for needed foreign goods which would cost it more to produce, can be attained only through free trade.

Under the gold standard economy, a nation finding itself slipping into a debtor position in international trade resorts to protective tariffs. Usually a considerable amount of controversy arises within the nation adopting tariffs regarding which industries are to be favoured and at which consumers' expense. What may seem fairest and in the best interests of the nation adopting the tariffs may appear as gross discrimination to the nation losing its foreign trade as the result of the tariffs. *Tariffs are one-way acting.* They constitute a one-sided departure from the nominal exchange rates of the currency unit. They make it more difficult for us to buy the foreigner's goods, but they do not make it easier for the foreigner to buy our goods. A much better course, if we are in the debtor position, would be to lower the exchange rate of our currency unit. This would not only reduce the purchasing power of our currency for foreign goods and thus reduce our imports, but it would increase the purchasing power of the foreigner's currency for our goods, thus increasing our exports and bringing to us the great advantage of free trade in being able to exchange goods costing us less to produce for foreign goods which would cost us more to produce. At the very best, protective tariffs are unscientific and unfair, but protection is a necessary expedient under the gold standard.

Tariffs tend to increase the cost of goods in terms of income, and, therefore, other factors being equal, tariffs tend to decrease the amount of goods which a nation can consume. In the long run, a reduction in the amount of goods a nation can consume means a reduction in the amount of goods that it can produce. Therefore, a nation will do best by adopting a policy which will permit the maximum consumption of goods.

A nation will consume the maximum amount of goods by being able to exchange freely the goods costing it less to produce for needed foreign goods which would cost it more to produce. Under a sound international exchange system which would permit absolutely free trade and keep each nation's exports balanced with its imports, the more foreign goods the people of any nation consumed, the greater would be the foreign demand for the goods which they produced. Hence, each nation will do best, in general, by discarding all tariffs and regulating the exchange rate of its currency, so that its payments made abroad will be balanced by the payments it receives from abroad.

If a nation were well adapted to produce certain goods that normally came to it from abroad, then a tariff for a time to protect such an industry while it was getting under way would be justified, but it must be remembered that a benefit to any of a nation's industries by a tariff is likely to be paid for by its consumers, thus reducing the total goods they can consume, i.e. reducing their standard of living.

So far as agriculture is concerned, with prosperity

ruling again throughout the world, farming is bound to become much more industrialized, and the standard of living of farm workers is bound to approximate more nearly to the standards of living of other industrial workers.

British agriculture has been in a bad way because of the more effective protection accorded British manufactures. Exports must be paid for by imports and the products of the more protected industries are exported and paid for by foreign goods against which the protection is less. Manufacturing has benefited at the expense of agriculture. If *all* British tariffs were discarded, in accordance with the plan developed in Chapter VIII, agriculture would then be on an even footing with all other British industries, and much of the land which is well suited to agricultural production—but which is now lying idle—would be producing healthy profits under modern methods and giving employment to agricultural workers under good standards of living.

For the best interests of all, each industry should stand on its feet and be independent of any artificial props.

In general, a nation would do best by devoting its energies to the production of goods in which it was best fitted to excel, and practising free trade.

It must be realized that the wages paid elsewhere would have absolutely no effect upon the standard of living of British workers, providing sterling's exchange rate were set so as to keep British exports in correct balance with British imports without any tariffs, and providing a sound policy with regard to

foreign investing were pursued. Then, in effect, foreign goods could be paid for only by British goods and incomes from existing British-owned foreign investments. The idea that sterling prices must be low in order to sell British goods abroad is a very harmful delusion which must be corrected. The reasons, and the advantages of free trade under a *natural* exchange rate of the currency unit, are pointed out in Chapter VIII.

To future generations, the idea of protective tariffs will appear as a crude makeshift of the unenlightened gold fallacy age—the age when in effect the essential commodities were bartered at widely varying exchange rates for a non-essential commodity, the non-essential commodity being in turn re-bartered for the essential commodities, and when hosts of willing workers in the midst of plenty were unable to exchange their labour for even the bare necessities of life.

Old Age and Disability Pensions for Workers.

The realization by the more developed nations that the services which a worker and a moneylender perform are both essentials in the production of commodities, and that the worker himself is no more a commodity than the moneylender is, is largely responsible for the breakdown of the gold standard economy. Much of our present disequilibrium is the result of the attempts to drive the gold standard in double harness with equity to the workers and moneylenders.

In an industrialized society, are not spenders as essential as savers?

For the maximum success under industrialization, should not spenders feel quite as secure against poverty in their declining years as the savers?

If a man goes through life as an honest worker, should he be faced with poverty in his old age simply because he has been a good provider for his family, or because he has been unfortunate with his savings? Has not his spending benefited all industry and enabled the saver to live his old age in ease? Should not each worker be able to look forward to a pension in his later life, the amount of which is in proportion to the amount earned during the productive years of his life? If all employers were required to pay a small tax on their payrolls for equitably providing for disability and old age benefits for all workers, to be disbursed by the Government, would not all commerce and industry be benefited by a greater freedom in spending? Would any injustice be done to any employer?

In order to keep the wheels of industry turning, it is important that the workers be afforded a certain amount of security for the time when they are unfit for employment, so that they may feel free to enjoy a good standard of living during their working years. The cost of taking care of old or disabled workers is logically a charge to the labour costs of production and should be reflected in the general price level. Such reflection would have no effect upon the cost of British goods, for instance, to foreign buyers under the correct exchange policy. The payment of old age and disability benefits is logically a Government obligation and therefore the Government should

raise the funds for such benefits by levying a small tax on all payrolls.

Privately conducted pension systems are decidedly wrong economically so far as the best interests of the community are concerned. They cause employers to give preference to the young when they take on new staff, even though older men and women are available, who are often better fitted for the work for five, ten, and fifteen years in many cases. There should be no economic reason for younger workers having preference over older workers while they are as well or better qualified for the work in question.

Under private pension schemes, new concerns, by selecting younger employees, have an advantage over old-established concerns which have important obligations to meet in old age benefits.

Then there is always a possibility that an industrial concern may be forced out of business, and become unable to meet its obligations to its former employees. Also the pensions paid through privately conducted pension schemes are often very small compared with the recipients' former remunerations.

Immigration.

As has been previously suggested, under the correct economy, a shortage of labour would be constantly felt. The first nation to adopt the correct economy for the Machine Age would find it advantageous to permit immigration, and its conditions would prove attractive to immigrants for a time. However, when one country gets well started under the correct economy other countries will be quick

to follow its example, and they would be loath to lose competent emigrants. They would prefer to enjoy for themselves the advantages to be derived from a high volume of consuming power, and a high volume of productive power resulting from a high volume of competent producers.

Under the correct economy each country would strive to make living conditions attractive to its own population, and most of its population would prefer to enjoy prosperity at home rather than in a foreign country. A shortage of workers is a condition which all nations would experience under the correct economy, and is a condition to which they would have to become accustomed, and for which they would have to allow intelligently in order to provide against a disturbance in their well-being.

Government Spending.

Government spending on public works, etc., for the purpose of giving employment to idle labour is a condition which would never be encountered in a nation operating under the correct economy.

In order to enjoy the highest standard of living there are certain facilities and services which can be provided for the benefit of all only through the expenditure of public funds.

In considering programmes for such expenditures the Government or the authorities responsible should always realize that the funds required could be made available for their improvement programmes only by reducing the money spent for goods and services or improvement programmes provided by private

enterprise, and they should always carefully consider whether the advantage to be gained would be justified by the sacrifice involved.

Programmes of public improvements should be planned with a view to dislocating private enterprise as little as possible consistent, of course, with the advantages to be gained from such improvements. In many cases it would be well to plan ahead with a view to keeping a certain amount of labour employed over long periods on public improvements.

A resort to the use of prison labour on public improvements would be very desirable, because in this way a reduction in the standard of living of those who pay taxes would be avoided to the extent that prison labour could be utilized. In general, under the correct economy, labour would always be in demand, and any workers, even though they paid no direct taxes, could gain nothing from the non-utilization of prison labour on public works.

Laissez-faire.

The doctrine of *laissez-faire* is all right up to a point. Its limitations become evident as industrialization progresses. In all games there must be rules for governing the conduct of the players. Likewise, in the greatest of all games, commerce and industry, there must be rules which will rationalize the conduct of all the participants to the end that all may derive the greatest possible satisfaction. Should not the Government assist the participants in arranging suitable rules for the

conduct of the game of commerce and industry, and act as an impartial umpire in the play of the game? Should it participate as a player also?

As the control of currency exercised by the central Government affects industry throughout the area using its currency, the rules and restrictions affecting industry should be consistent throughout the nation, and, as is stated elsewhere, if the people of any country are ever *right* in thinking that for the best interests of all concerned their country is too large to allow the central Government to have final discretion over all the factors which determine the buying power of its currency and the balance between the consuming power and productive power of the country as a whole, then that country is too large for one central Government and one currency system in the Machine Age.

The Profit Motive.

All those who engage in commercial pursuits naturally expect to reap more than they sow. "Viewing men as they appear in the world about us and as they are revealed in History, the hope of profit seems quite as universal a force in human nature as gravity is in the physical world. To carry this analogy further it may be recalled that the force of gravity serves faithfully and well those who understand its laws; and it is not too much to hope that the same may be said of the profit motive.

"What we mean by profit may be subject to many interpretations. The term may be used broadly enough to cover any benefit or advance or progress,

or so narrowly as to exclude everything but the money profit from individual commercial transactions. It may cover short or long term periods. It may apply to a given person or to society as a whole. It may be selfish or altruistic. It may be the reward of righteous and noble living no less than the clipping of coins by the money changer. We may examine its ethical or its economic significance, or we may attempt to reconcile both in a code of social conduct. In any event we must deal with it, and it is the part of wisdom to deal with it realistically and with understanding. We cannot eliminate it." [1]

The profit motive which translates itself into stewardship over vast productive enterprises by those best suited for such responsibilities and who devote their profits to more and better productive facilities is a force to be utilized to the fullest if the luxuries of to-day are to be made the necessities of to-morrow with a minimum of unproductive effort.

The profit motive with its constant urge for better and better efficiency and the avoidance of mistakes uncovers genius for organizing, discriminating between promising and unpromising new ideas and projects, acquiring capital for the development of the promising ones, etc., that would often never come to light under a bureaucratic and division of responsibility system dominated by political considerations.

The most capable organizers and executives are often devoid of qualities which would enable

[1] Mechanical Engineering, July, 1935

them to function as leaders under the petty hindrances of political domination where vote-getting ability and personal charm often outweigh fitness for rendering the particular services required.

Productive power has been out of step with consuming power so often and so long under the gold standard economy that many have come to believe that this flaw is inherent in the utilization of the profit motive whereas all that is required is an economy which will permit the profit motive to be utilized to the utmost under a constant balance between productive and consuming power.

Free rein for the profit motive under economic liberty and dominated by supply and demand and the survival of the fittest is the surest and speediest way to raise the standard of living if the Government will merely assume its responsibility of keeping demand in general in step with supply by supervision over the buying power and exchange rates of its currency unit.

No Altruism Involved in Practice of Correct Economy.

Everyone wants and is entitled to a standard of living in keeping with his desire and ability to produce. The benefits to all from freedom for individual initiative have long been recognized, but the enjoyment of those benefits has been limited because of an economic system which permits private enterprise to increase the power to produce without a corresponding increase in the power to consume. Therefore many have thought that the correction lies along the line of curbing individual initiative.

However, all can enjoy the highest possible standard of living only if the benefits of private enterprise are utilized to the utmost, and if the danger of consuming power falling behind productive power is eliminated.

Man is by nature selfish, but with foreign investing ruled out, a producer can achieve the greatest prosperity in the long run only as the prosperity of others increases. Our economy, to be correct, must utilize the economic instinct of the individual to the end that he can increase his prosperity as he renders services which will increase the well-being of others.

If producers are to prosper, consumers must prosper, and therefore their interests are mutual, and therefore in theory the interests of labour and capital are mutual under industrialization. For any nation to make practice accord with theory, the simple requirements are a currency unit of constant purchasing power within its confines, and the proper balancing of its exports by imports. The effects of these requirements would not savour of altruism in the least. They would merely allow the natural desire for higher incomes by all producers to be realized to the fullest extent possible in the existing stage of industrial development.

As producers are now constituted, to allow the free play of the forces arising from the desire for higher profits and higher wages and salaries is the surest road to higher efficiency. Higher efficiency is the only possible road to the enjoyment of more and more goods and leisure by all.

A currency unit of constant purchasing power, by the only possible means, would merely enable the desire for higher incomes to be translated freely into higher efficiency at the maximum rate compatible with a balance between consumption and production that would ensure full employment with a rising volume of profits for capital, and full employment with a rising rate of pay for all workers. The greater the desire for higher incomes by producers, the higher would be the efficiency in every branch of commerce and industry, and therefore the higher would be the standard of living for all.

Capitalism and Socialism.

Funds become available for investment in more and better productive facilities, in the long run, only as there is saving and abstinence from spending, and not by printing money, as some people would have us believe. This holds, regardless of whether private enterprise or the Government provides the productive facilities. Only voluntary savings are available to private enterprise, while the Government may borrow voluntary savings or it may levy taxes to raise funds for providing the productive facilities. In either case, however, there is the same abstinence from spending, voluntary or involuntary.

As the public only eats, wears or uses and enjoys goods and services the public is interested in who produces them *only to the extent that they are always produced as efficiently as possible.* The higher the efficiency of production, the more goods and services all will be able to enjoy. Therefore, it is to the interest

of all that, in those fields where free competition can bring about the highest efficiency in production and in the development of new inventions, etc., private enterprise should rule, and likewise in the fields which are natural monopolies, such as the public services, where free competition cannot give the best and most efficient services, Government ownership or Government control should rule. In Government-owned projects, private enterprise almost invariably provides the equipment used, under keen competition, and the Government is thus enabled to benefit from the best research in the special fields and take advantage of the latest developments. As a rule, in Government-owned projects Government management is confined almost entirely to the management of operations, and, as there are generally similar operations under private enterprise, private management sets the pace for Government management, and in most cases the Government operation of natural monopolies leaves little to be desired from the standpoint of good service and its cost.

With the Government owning or controlling only natural monopolies in the field of production and *providing a currency unit of constant purchasing power by the only possible means* under free competition, and suitable old-age and disability pensions, the author believes that the workers would be provided with about all the socialism they would ever want.[1]

[1] The workers should, of course, be afforded more rationalism in the control over the exchange rates of the currency unit and the volume of bank credit and currency outstanding; also workers should not be compelled to take lower wages and salaries in order to premit foreign investment. These are dealt with in subsequent chapters.

And, similarly, he believes that, as these measures would ensure a consuming power always in step with the full productive power on the whole and always a good demand for capital and labour, thus ensuring the widest possible economic liberty for the individual, *entrepreneurs* and capitalists would be provided with about all the capitalism they would ever want and could consistently ask for.

When consuming power is out of step with productive power and unemployment is ruling extensively, there is seldom complaint about the spending of the rich because the more they spend the more employment there is for labour. With consuming power in step with productive power, the situation would be changed. Then if it were customary for the moneyed classes to live lavishly and extravagantly, the goods and services which would be available for fulfilling the simpler wants of the poorer classes would naturally be reduced and a social problem would arise—not an economic problem.

In such an event, the economy should not be upset and the position of *all* the moneyed people should not be impaired in order to penalize the offenders, but instead, the offenders should be dealt with directly by suitable special taxes on their extravagances and wasteful uses of their country's resources.[1]

[1] With wages, profits and interest being always allocated in harmony with sound economic principles, savings would always be in high demand, as is pointed out in Chapter VII, and this would tend to operate as a deterrent to extravagant living by the moneyed classes.

CHAPTER V

ECONOMIC POLICIES OF GREAT BRITAIN SUBSEQUENT TO THE OUTBREAK OF THE WAR[1]

WITH the outbreak of the War it was immediately apparent to Great Britain that the gold reserves on hand were not sufficient to afford the usually accepted gold backing under the gold standard for the greater amount of currency that would be required for the much greater industrial and commercial activity incident to the unhampered prosecution of the War. Great Britain's currency was therefore immediately cut loose from gold, and made a credit currency pure and simple.

With the new life taken on by Great Britain's industry and commerce, large profits began to accrue to most industrial and commercial enterprises, and as there was a shortage of labour, increases in wages were allowed. Higher wages increased the cost of producing goods, and the purchasing power of the pound was therefore correspondingly lowered.

Great Britain emerged from the War with a credit currency which had effectively served all legitimate needs in a period of the greatest commercial and industrial activity in her history. The purchasing power of the pound at the end of the War was less than at the beginning of the War, but this was fully accounted for by natural and obvious reasons.

[1] Readers of this chapter are reminded of the second paragraph in Chapter II.

Fortunately during the War and for some months after, intelligence was exercised by Great Britain's Treasury in mastering sterling's international exchange rate. The importance of this will be apparent later.

In spite of the fact that during the War a large part of industry's products was consumed on the battlefields and by those engaged in war activities who gave no goods in return, the advantage of better efficiency and volume production from the full employment of labour and capital was sufficient to permit *higher wages* with higher standards of living for the workers. There was full employment for labour and capital because there was buying power for all that Great Britain could produce.

Unfortunately, at the close of the War it was not realized that the restrictions placed upon international exchange contributed much to the health of commerce and industry during the War. The Government was induced to give up its control of the international exchange rate of its own currency, and the pound was "allowed to find its own level" through the haphazard influences of international trade, international investment and speculation through international exchange.

While other European nations were easing or writing-off the burden of their war and other internal debts by inflation, a cry went up in Great Britain for deflation, and "the pound must look the dollar in the face again," and a high bank rate—a very effective deflationary expedient—was used. Deflation always brings unemployment, and the obligation

to provide for the unemployed returned soldiers resulted in the extension of the system of National Unemployment Insurance to all industrial workers. Sterling was finally manœuvred back again on to the gold standard in 1925 at the old parity, thereby greatly increasing the burden of Britain's internal debt, with the result that in spite of almost intolerable taxation the tremendous internal War debt, more than sixteen years after the close of the War, stands at about the original figures, with its burden becoming heavier almost every year until the year 1934.

This move back to the old gold parity gave sterling greater purchasing power *for foreign goods*, and increased the gold cost of British-made goods to foreign purchasers, and an increased excess of imports over exports in goods was a natural consequence. British productive activities and the resources over which the heavy tax burden could be spread decreased, unemployment increased, and Great Britain's gold reserves began to dwindle.

The Fallacy of Borrowing Gold.

Great Britain borrowed gold or gold credit for the purpose of "stabilizing its currency." But the high bank rate or rediscount rate which makes such borrowing feasible under the gold standard results in deflation, and a higher cost for the currency and credit accommodation required for financing production. The effects of a gold loan to a debtor nation generally operate to make it still more difficult for the debtor nation to gain favourable balances in

international dealings, which are in the end the only means by which a nation's external debts can be paid.

When a nation in financial difficulties resorts to playing the international gold standard game with international bankers, its luck seldom changes. The outside lenders of gold credit may not always win, but the borrowing nation generally loses. A little consideration will reveal that the gold standard generally takes from him that hath not and gives to him that hath.

The weakness of the credit structures of some of the other European nations increased Great Britain's difficulties, and Great Britain was experiencing all the ills common to distressed debtor nations of the past under the gold standard, except a most important one—*there was no hunger.* According to the gold standard economy, unemployment must always bring hunger. Economists have contended that for a semblance of industrial equilibrium there must be a sufficiently wide stratum of society so destitute or living so close to its income that unemployment will always quickly bring about acceptance of lower wages. But in the case of Great Britain, the National Unemployment Insurance scheme had become so firmly established that sufficient pressure could not be exerted in the old way to force wages down to correspond with the increased gold value of sterling. While lower wages would have lowered sterling prices and corrected Great Britain's trade balance, the creditors and *rentiers* would have been inequitably enriched at the expense of the many, and the

burden of the public debt, in terms of the goods required to pay it, would have been further increased.

Deadlock between Great Britain's Conflicting Interests in Monetary Policy Most Destructive.

With labour enabled to keep wages firm, sterling had to weaken, and was finally forced off the gold standard again in September, 1931.[1] Thus the slight degree of mercy and justice rendered to the unfortunate unemployed of Great Britain proved more than the gold standard, which must be free from such considerations, could withstand.

The deadlock between the opposing interests has cost Great Britain very dearly in many ways. However, if an obvious lesson is well learned, the sacrifices of the past can soon be bearing abundant fruit, and the initiation of the much-frowned-upon but soundly humane British dole may yet be acclaimed the greatest forward step in all history to lasting prosperity and world peace.

The PARAMOUNT lesson to be learned from Great Britain's costly experience, however, is that the control of the purchasing power of any currency for any length of time is impossible without AGREEMENT between the conflicting interests.

[1] The flight of funds from Great Britain was the immediate cause of sterling being forced off the gold standard. The fear that Great Britain would be forced off the gold standard was the cause of the flight of funds from Great Britain. And the fact that Great Britain was not able to force low enough wages and prices in terms of gold to prevent the continual loss of gold in her international trade account caused the fear that Great Britain would be forced off the gold standard. To insist that Great Britain was forced off the gold standard because of the flight of funds from Great Britain or because others failed to observe the niceties in the gold standard technique is typical of the shallow thinking by many who would be expected to think more deeply.

Coincident with the announcement that sterling was off the gold standard, the rediscount rate was raised to 6 per cent as an heroic measure for propping up sterling's purchasing power. The immediate object was to make London attractive to floating funds and thus improve the sterling exchange rate. The drastically high bank rate, however, caused a pressure for deflation more distressing than any previous measures for maintaining sterling upon the gold standard, and, as always, a policy which adversely affects industry and commerce proves short-sighted and only saps the vitality of the nation. A better way of controlling a currency's exchange rate is discussed in Chapters VIII and IX.

The Mistakes of Previous Generations are Being Visited upon Great Britain's Present Generation.

During the development of industrialization in Great Britain there was often sufficient consuming power at home and abroad to absorb all that British industry could produce. British foreign investing was freely encouraged, and was the sustaining power behind foreign buying.

Whenever British exports failed to balance British foreign investments and payments for imports, the banks began to lose gold. If this continued far, the bank rate was raised and the volume of bank credit outstanding was contracted. This forced debtors to reduce prices and reduce their commitments in order to meet their obligations at the banks, and it seemed natural to let the vicious circle of lower prices, lower employment, and lower wages operate,

until lower prices attracted more buying from abroad.

Under this system, no matter how great the investment abroad, and regardless of the suffering caused at home, British wages and prices could always be relied upon to fall to a level that would permit the foreign investments to be paid in goods without the ultimate loss of gold.

With the above economy in vogue, production seemed limited only by production costs. Therefore employers kept wages as low as possible, and any loss to the home consuming power through low wages was offset by the profits accruing for investment abroad and for thus increasing the foreigner's consuming power for British goods.

During the operation of that economy Great Britain produced much more than she consumed, but it was pursued so long that the incomes from British foreign investments, which are paid in goods, have been compelling Great Britain to consume materially more than she produces.

Great Britain has been unable to gain favourable trade balances in goods and services for many years, and her gold reserves have been maintained by the incomes of her people from foreign investments.

In the nineteenth century vast private fortunes were built up through the industrialization of Great Britain and the exploitation of the workers who, under the operation of the gold standard, functioned economically as commodities. The workers were denied sufficient wages to keep British production of

goods and services balanced by British consumption; but this handicap to the industrialists was overcome by investing and selling abroad in the newer nations and dominions, and vast excesses of exports over imports were Great Britain's lot in international trade. Great Britain's industrialists and moneyed classes did very well in this manner for many decades. Later, however, as her erstwhile customers, the newer nations and dominions, developed, they preferred to manufacture for themselves. To make the return of income upon the British-owned investments they had to resort to the sound expedient, under the unsound gold standard, of protective tariffs, so as to cause their exports of goods to exceed their imports. Through the operation of these tariffs the credit accruing to Great Britain from her foreign investments was offset by her payments to meet adverse international trade balances in goods and services.

The U.S. particularly profited from Great Britain's fallacious policy of investing abroad. Some of Great Britain's early foreign investments were made in developing resources of the U.S., and thus raising the standard of living in the U.S. In later years the U.S. paid for these benefits by an excess of exports over imports in her trade with Great Britain, which the payment of returns on British investments under the U.S. tariff policy permitted.

The denial of purchasing power to Great Britain's workers for a number of generations permitted a vast excess of exports over imports in goods and services. This not only deprived those workers of equity

in the distribution of the fruits of their industry, but the foreign incomes which have resulted from that practice and which are paid in goods have been preventing the workers of the present generation from getting an income from the production of goods equal to the labour costs of the goods consumed in their own country. Under the latter condition, capital invested in industry has had to suffer similarly with labour.

The low-wage and foreign-investment economy required drastic reductions in prices periodically. It can never be restored because the amount prices can fall without reducing wages is limited, and with the advent of collective bargaining and the dole, unemployment no longer brings the old fear of hunger and the acceptance of lower wages.

It has become plainly evident that the tendency in industry is always towards higher efficiency, and that the standard of living of the workers should be rising and never falling. Therefore workers naturally rebel against lower wages, and thus the low-wage foreign-investment economy can never be restored for any length of time.

Great Britain Tries Protective Tariffs.

When Great Britain realized the gravity of allowing her imports of goods and services to exceed her exports of these by such a wide margin, the McKenna duties were inaugurated. But they alone were not sufficient to overcome the measures taken by other nations and dominions to prevent the loss of gold, and the need for still higher duties in Great Britain

was felt. Even many of the die-hard free traders who knew that protection cannot bring about the ideal condition for any nation, became favourable to more protection, and, since sterling went off the gold standard, a great number of additional protective duties have been inaugurated. However, to a considerable extent, the stable was locked after the horse was stolen.

For the best interests of any nation, the imports of goods which would cost it more to produce should just balance the exports of goods costing it less to produce. If the international movements of private wealth were kept balanced, this desirable balance in the exchange of goods and services would almost automatically follow. However, we labour under the delusion that private wealth should be unhampered in its movements from one nation to another regardless of the ultimate consequences upon the economic well-being of the nation losing it, yet workers are denied such freedom.

In a nation off the gold standard, protective tariffs benefit those desiring to export private wealth and those who desire to eliminate foreign competition, but the benefits to the few are paid for, in the long run, by the many—the consumers.

At the Ottawa Conference, after much debate and deliberation, a compromise was reached which, it was hoped, would result in mutual benefits to Great Britain and the commonwealths concerned.

However, for Great Britain, for instance, to agree to pay Canada a yearly amount for wheat in excess of what she would have to pay the U.S., Great

Britain has to be satisfied that Canada will pay her a similar yearly amount for certain of Britain's products in excess of what Canada would have to pay the U.S.

No matter how carefully they may have worked out a system of tariff preferences between themselves against the rest of the world, one is almost sure to benefit at the expense of another, and for this reason such bargains are unsound and unsatisfactory. In resorting to such makeshift measures there is not only a conflict of interests between the commonwealths themselves, but there is a serious internal conflict in each commonwealth. It is difficult for the consumers of Great Britain to see the advantage of paying more for foreign wheat in order to increase the profits to British farmers. Likewise it is difficult for Canadian manufacturers to understand why they should have protection from American manufacturers and not protection from British manufacturers, in order to benefit the Canadian wheat growers.

The fact is, no special economic community of interests exists between any two commonwealths having separately controlled currency systems. Under a sound international exchange system, as will become evident later, each independent commonwealth or nation would do best by avoiding any preferential trade agreements with any other country whatsoever. Each country would enjoy the greatest consumption of goods—the highest standard of living—by free trade with the rest of the world.

Tariff preferential agreements between any of the

members of the British Commonwealth of Nations cannot possibly operate to their mutual advantage, and are bound to create dissatisfaction and bad feeling sooner or later. The bond of union will remain stronger and each will be of more assistance to the others, should the hour of need ever come, if each is entirely free from any economic restraint.

Is Great Britain in Danger of Becoming a Decadent Nation?

Great Britain built up a great Empire, the impelling object being to build up a vast free trade area. The Colonies have found that free trade under the gold standard is inimical to their best interests. Also British capital and labour have found that the old low-wage free-trade economy is seriously detrimental to their best interests, and Great Britain is realizing that overseas possessions are not a great commercial asset.

The fact is that Colonial possessions are a liability economically rather than an asset to the Mother country. They appear attractive at times as they afford an outlet for capital, in the form of goods, which is not finding profitable employment at home simply because of a defective economy at home.

As Colonies develop they reach a stage where they feel that they should be on an even footing, economically at least, with the Mother country, and they resent any parental restrictions giving her economic advantages which operate in any way to their disadvantage.

The world impression is that Great Britain's hold

on her Colonies is weakening, and some have said that she is becoming a decadent nation. If Great Britain's moral hold on her Colonies and dominions is weakening it is because of faulty economics. Furthermore, if the lack of an opportunity to perform useful work by an appreciable percentage of her population over a long period will cause decadence, then Great Britain is in danger of becoming a decadent nation also through faulty economics.

The Urgent Need.

While the people of Great Britain are still enjoying as much freedom as is enjoyed in any country, they are not happy, and are dissatisfied with an economy which causes so much unemployment of labour and capital. The advantages of Great Britain's brand of democracy have not been sufficient in the eyes of other countries to prevent the adoption of Dictatorships in the hope of correcting the economic difficulties with which they have been beset—difficulties which resulted from the loss of balance between consuming power and productive power and the fallacious belief that interference with supply and demand is the palliative for that calamity. Allowing profit without competition is the road to dictatorship and the loss of civic as well as economic liberty.

In one breath dictators point to a need for greater population and urge fecundity, and almost in the next they strive to create a patriotic fervour for Colonies as a solution for over-population from which they claim to be suffering.

The present undeveloped areas are unsuited climtically for colonization by Northern races to any extent, and any raw materials which might be developed in them can be, on the whole, obtained in world marketsfar more advantageously economically.

The wants and consuming power of its own people will be beyond the productive power of any country if it will merely put its own economic house in order, and it could then develop a foreign colony only by lowering its own standard of living.

These Dictators are not able to interpret the significance of the economic factors involved in the History of the past any better than the leaders of democracies. They do not realize the ill effects to a country resulting from first producing much more than it consumes over a long period, as it does when it develops a new territory, and then later consuming more than it produces, as it does when it receives income on its previous investments under the gold standard economy. They may recognize that man's natural desire to produce and consume is thwarted by the tentacles of the gold standard, but if they do they are unable to point to the correct substitute.

Naturally they feel a desperate need for a consuming power to match their potential productive power, and, in view of the failure of other countries to achieve prosperity and in view of the trend towards Economic Nationalism, they believe that their best chance of success lies in increasing their free trade area through the expansion of their own domains. They may realize that free trade with the whole

world would be a vastly greater advantage to all their people, but if they do, they do not know how that desirable end is to be achieved. The most that they can glean from the economics of the past is that might makes right, for a time at least.

Furthermore, when a country not rich in raw materials is prevented by tariffs from exchanging its manufactures for raw materials at their respective natural values in world markets, that country has a complaint against the world order and seemingly an excuse for not abiding by idealistic standards of international conduct.

Only some straight economic thinking can prevent the History of our age from continuing the History of the rise and fall of nations. The need is URGENT.

While Great Britain may not be in immediate danger of a Dictatorship and the complete loss of economic liberty, she is in danger of war if she, or some other country, does not soon demonstrate the only way a consuming power to match the full productive power of a country can be maintained under economic liberty, and free trade with all the world.

Need for Raw Materials.

The fact that Great Britain does not have the same resources in raw materials as America, for instance, is not a handicap to the enjoyment of a standard of living just as high as America could enjoy. The raw materials required in the production of finished goods are only a small part of the cost of the finished products. The cost of the raw wheat

required for a loaf of bread probably does not exceed 10 per cent of the cost of the loaf to the consumer. The cost of the raw copper in electrical apparatus is a very small percentage of the cost of the finished article. The amount of finished goods Great Britain needs to exchange for the necessary raw materials is a very small percentage of the value of the finished goods which Great Britain produces. To enjoy the highest standard of living Great Britain will do best by exchanging goods she is well adapted to produce for the needed raw materials and food from abroad, rather than by trying to use substitutes for them which would cost her more to produce.

Great Britain is not self-contained, and requires certain raw products and materials from abroad for which she can always readily exchange finished goods. She has valuable resources in coal, iron, and other materials, and in the intelligence and ambitions of her people. If previous Governments had been more concerned about the ultimate effects of foreign investments, Great Britain would have led the world in her standard of living, as she could now, under the correct economy for industrialization. This is not intended as a condemnation of individuals, but rather as a condemnation of a theory which has been too long in vogue. In our eagerness for outlets for our energies, we naturally adapt ourselves to conditions as we find them, and not to conditions which should, but do not, exist.

The standard of living *in any country* need not suffer because needed raw materials cannot be produced within its confines.

The Starting Point for Prosperity.

For a time it seemed as if Great Britain had lost by the arrangements made with other nations, which provide that the War debts owing to her are to be paid in sterling, while the amounts she owes are to be paid in gold. But foreign obligations can in the end be paid only by goods and services. The ease with which foreign obligations can be paid in goods and services, depends upon the health of industry and commerce in Great Britain.

The high market value of low interest-bearing Government securities, and the success of Treasury conversion schemes are pointed to with pride in certain quarters in Great Britain and other nations, whereas a vastly healthier condition of the source of their life blood—their commerce and industry—would be indicated if such low interest-bearing securities were selling at two-thirds their par values.

The conversion schemes were possible because of the operation of a grossly faulty economic system which produced a glut of unemployed funds. Failure to bring consuming power into step with productive power, and price fixing and restriction of output greatly weakened the natural attraction between idle capital and idle labour. When the former higher price level is restored and prosperity is achieved the Government, with proper regard for its credit and with justice to its creditors, should restore the former higher interest rates of its long term obligations, to the extent that their market values will approximate to their par values.

Also there has been a source of pride in certain quarters from the fact that certain currencies off the gold standard have been tied to sterling. The exchange rates being adopted, however, are intended to prevent unfavourable trade balances to the commonwealths tying to sterling. To avoid injury, Great Britain may have to combat such tactics by tariff adjustments. She would do much better, however, by adopting a correct international exchange policy.

Great Britain, like all other nations, is in dire need of "reflation," which could be obtained soundly, quickly, and exactly to the desired extent.

Whenever Great Britain has enjoyed prosperity heretofore, except during the War, she has depended upon the foreigner's power to consume along with her own to balance her power to produce. The fallacy of this practice is now apparent. Foreign investments made it possible for a time, but the incomes from these now prevent Great Britain's industry from enjoying a market even equal to her own consumption. Great Britain must realize that her ability to produce is now limited solely by her own ability to consume.

Great Britain's industrialists are limited in the goods they can produce for home consumption by the consuming power at home. They also are limited in the goods they can export by the consuming power at home for foreign goods.

The starting-point for prosperity in any nation under present conditions is to increase the consuming power at home. Building up the consuming power

at home is the only possible way out of the present difficulty, and *maintaining a high consuming power at home is the only means of maintaining prosperity in any nation*, now or in the future.

Foreign Investing is Wrong[1]—Home Buying Power the Essential for Export Trade

The suggestion is often made that the remedy for the anomaly of idle labour and idle capital in Great Britain is emigration and foreign investing. But to send British labour abroad is to reduce the potential productive and *consuming* power of Britain. To export idle capital is to lose capital which should be finding highly profitable employment by combining with idle labour to provide facilities necessary for a higher standard of living in Great Britain. Furthermore, to export capital is to add to the present excessive volume of foreign investments the incomes from which can be paid only in goods. Receiving goods from abroad for which no British goods can be exchanged already handicaps British industry by preventing it from producing the equivalent of all the goods consumed in Great Britain.

Regardless of where goods are consumed, the country which produces them always furnishes the buying power for them in the long run. If goods are exported the country which produces them must furnish buying power for the imports which pay for them, or if a country exports more than it imports, it must loan and/or invest abroad, or it must pay

[1] Foreign investing is more particularly dealt with in Chapter X.

interest, etc., on foreign loans or investments previously made in it, in order to finance the foreign buying power for its excess of exports over imports.

For many decades Great Britain produced much more than she consumed by keeping wages low and furnishing foreign buying power for her goods through investing profits abroad. The former policy of low wages and the investment of profits abroad has proved short-sighted. If it had been pursued long enough the time would have come when foreign incomes would have brought into Great Britain all the goods for which there would have been consuming power, and there would have been no employment for capital or labour in the production of goods.

Low wages and investing abroad hold the home consuming power down, thus reducing the opportunities to all those who cater to the home market and the home consuming power.

In order to give employment to its own capital and labour every country is now anxious to produce at least the equivalent of all it consumes, and therefore any worthwhile equilibrium in industry is no longer possible through the low-wage foreign-investment system.

Under the gold standard economy, the lower the standard of living of the workers of an industrialized nation was, the more it could normally export abroad.

Under the correct economy, the higher the standard of living of the workers of an industrialized

nation is, the more it will export in exchange for imports.

The conditions favourable to prosperity through the low-wage foreign-investing economy, in other words the gold standard economy, have passed for all time. Now each nation is dependent solely upon a consuming power within itself for restoring and maintaining its prosperity.

Great Britain's Government-interference Economy.

Great Britain has been enjoying better trade, and the belief that Great Britain is better off than any other nation is prevalent, and is probably true, but that is not saying very much. The people of Great Britain are paying very high taxes and are increasing their total outlay out of public funds, direct and indirect, for unemployment relief.

Ever since the low-wage foreign-investment economy became no longer operative, the consuming power for British goods has been badly out of step with British potential productive power. To allow or enforce free competition when consuming power is out of step with productive power would start again the vicious circle of lower prices, lower employment, and lower and lower consuming power. So the Government sanctions price-fixing, restriction of output, marketing boards, etc., and doles are paid to both labour and capital.

Altogether the present-day government-interference economy is a far cry from the pre-War economy. Also it is a far cry from the correct economy.

Great Britain is limited in the goods she can

soundly export by the buying power at home for imports, but, if the buying power at home were properly organized, imports would be desired to an extent that an export trade greatly exceeding that of any previous period in Great Britain's history would soon result.

Consider for a moment the potentiality of the home buying power—

There is now a vast army on the dole and another army which is being afforded relief under the poor law, many of the members of which are able-bodied and desire remunerative employment. All these comprise the officially unemployed. Then there are the unofficially unemployed—the many men and women who are being supported by relatives and friends and the many on small incomes and pensions who are able-bodied and desire to produce and enjoy a higher standard of living.

Many of the employed are working with inefficient tools, and their consuming power is low because their productive power is low.

Compare the present home market for British goods and foreign goods and opportunity for profit in producing goods for home consumption and foreign consumption with what they would be if all those mentioned were producing under the most efficient methods and if wages and salaries were being paid on a scale that would keep the consuming power in balance with the full productive power! Think of the profit in sight for British capital in providing the latest and most efficient productive facilities in every branch of British industry, for

which there would be an ever increasing demand under the correct economy!

Experience in the United States proves that when full employment under free competition rules, technological improvements in production progress rapidly. Under the correct economy the productive capacity and the standard of living in Great Britain would advance by leaps and bounds.[1]

Many in Great Britain are complaining of "Economic Nationalism." Those having in mind the foreign tariff barriers against British exports have some justification for their complaint, except that raising British barriers against imports is the wrong way[2] to lower the foreign barriers against exports. Those having in mind the bar to foreign investing are short-sighted and have no justification for their complaint. If "Economic Nationalism" means reserving the capital of each nation for the use of its own people in order that they may enjoy a standard of living in keeping with its full productive power, then "Economic Nationalism" has probably come to

[1] The productive power of a country is dependent upon the consuming power for its products. The funds which become available for increasing its productive power come from the part in the selling prices of goods which is saved for that purpose, and the greater the volume of goods produced and sold, the greater becomes the demand and the opportunity for profitable employment for savings to increase productive power.

Under the old low-wage economy which required selling and investing abroad, savings were used partly for furnishing the foreign buying power for the surplus of exports over imports, and partly for increasing the productive power at home. In the practice of that economy there were necessarily many ups and downs in the total volume of production, and industry was functioning at its best only a part of the time. Under an economy which ensured constant equilibrium between consuming power and productive power under free competition, industry would be constantly functioning at its best and therefore the conditions favourable to the development of productive power at the highest rate possible would be constantly ruling.

[2] The correct way is explained on page 263.

stay. Under the correct economy there would always be a high demand for British capital for home enterprises.

Great Britain has been enjoying some revival in trade due to the effect of her higher tariffs, and the former lower gold parity of the pound. Also the effects of Government spending for armaments have been noticeable.

Prices in certain instances have been held firm through the operations of speculators' pools. These are harmful to the health of industry and the need for curbing such operations is mentioned in Chapter VII.

The industries which are producing goods that were formerly imported from abroad are enjoying greater activity, and in many cases they are being expanded. Capital goods industries have been benefiting from this situation, and more labour has been in demand for building and equipping factories and factory extensions, etc. On the other hand, the industries, the products of which formerly went abroad to pay for British imports, are now very much depressed, and the net effect is that unemployment has not been very materially reduced. The tariffs have helped certain industries at the expense of others—coal, textiles, shipping, etc.

The producers and distributors of certain products have been enjoying better returns through the shutting out of foreign competition and the more effective operation of their own price-fixing associations, but such benefits are at the expense of the energizing force in trade to be derived from free

competition when the consuming power is in balance with the power to produce.

Among those who operate under price-fixing associations and marketing boards, "co-operation" is the magic word which the many who are dissatisfied are asked to consider by their officials. But when "co-operation" means that one must conduct his business on an artificial basis, and that he cannot reduce his prices in order to clear his stock, or prevent the waste of useful products, and that he must work his well-equipped plant at part capacity in order that a high cost producer may continue to operate, "co-operation" affords him very little solace.

Such "co-operation" is *sterilization* of industry, not "*rationalization*," the high-sounding word which has been grossly misused for cloaking the unsound and short-sighted economic practices which stifle competition in British industry.

When capitalists are rewarded for the services they render society without competition, it is impossible to determine where a just profit ends and "graft" begins, and the practice of that economy results in the worst of all economic misfortunes—the serious weakening of the natural attraction between idle capital and idle labour. Capitalism without free competition ceases to be capitalism and becomes privilege, and a more harmful "ism" for the affliction of society can scarcely be imagined.

When the Government sanctions cartels, marketing boards, price-fixing, restriction of output, etc., the tendency is to set prices artificially at levels

which will ensure profits as high as industrialists and Government agents think the public will stand.

When free competition is really ruling in any industry, the profits made are almost never questioned by the public. Free competition stimulates the development of better methods, and thus enables a greater output of the products of industry to be made at a relatively lower cost.

When price-fixing and/or allocation of output are resorted to for ensuring a profit the benefits to be derived from the profit motive are lost and therefore the excuse for permitting profit is lost. There is little if any argument against Government ownership in privately-owned industries which resort to price-fixing and/or allocation of output to ensure profit.

What justification is there for profit and what is the formula which should determine the amount derived without competition? What formula should determine wages, and what formula should determine prices? Under Government control dilemmas are constantly encountered which cannot be solved to anyone's satisfaction for any length of time.

Under Government ownership or under price-fixing in private ownership the benefits to be derived from the urge to use the most efficient productive facilities, which is inherent in competitive industry, are largely lost. Under either system high incomes can be obtained by the leaders only through the exercise of a high order of political skill. Under such conditions profits appear very little different from graft to the public, and it is not surprising that

many strongly favour Government ownership. Under Government ownership high incomes would be honestly possible only through high salaries, and the masses could well feel that they would be less exploited under Government ownership than under private ownership which is devoid of competition.

Unless the fallacy of treating the symptoms of depression instead of the cause is recognized, bureaucratic control and Government ownership will follow Government sanction of price-fixing as logically and as surely as night follows day.

If British industrialists persist in looking no further than the ends of their noses, true capitalism, which is really economic liberty, is in grave danger of receiving a blow from which it will not easily recover. Democracy cannot long exist without economic liberty.

When the power of the country to produce exceeds its power to consume, an artificial measure is required to prevent harm from the downward trend of prices which would otherwise result from that condition under free competition, but the Government provides the wrong artificial measure. Instead of its lending a hand to prevent the action of free competition in the production and marketing of each of the various important commodities, the Government should merely lend its hand toward bringing the consuming power of the country as a whole into step with its productive power. Then economic liberty and the great benefits from free competition, which is the life of trade, could function in bringing prosperity to all.

As suggested, certain of great Britain's capital goods industries have been benefiting from the demand for more capital goods, but a prosperity which is based upon the production of capital goods cannot continue long if the consuming power is not forthcoming for the resulting consumers' goods.

Furthermore, the price-fixing associations which are operating in Great Britain tend to reduce the demand for capital goods, and therefore weaken the natural attraction between idle capital and idle labour.

As an example of the natural attraction between idle capital and idle labour under free competition, the case of the Rhodesian copper development may be mentioned. The copper market has been in a very depressed condition for five years, yet at the present time certain interests are spending large sums of capital they have recently raised in order to increase and improve the facilities for producing copper in Rhodesia. This procedure, which is giving employment to capital and labour in Great Britain and Rhodesia, *and which is increasing the consumption of copper*, would be impossible if the companies operating in Rhodesia were bound by a price-fixing association which would prevent them from underbidding their competitors in order to ensure capacity production.[1]

Great Britain has enjoyed some benefit from the gold boom which is taking place in Africa, but there

[1] Since the above was written the copper producers of the world have agreed upon certain allocations of production, with the result that new facilities referred to are idle. Also certain other projects which were planned are being held in abeyance and thus employment for capital and labour in the production of producers' goods is being withheld.

is no hope for prosperity in Great Britain while importance is attached to the amount of gold the pound sterling will buy. The time has come when Great Britain's only hope for prosperity is through the realization that the buying power of the pound and her balance between productive capacity and consuming power depend upon the general wage and salary level in Great Britain.

There is such a glut of idle funds[1] seeking employment that industrial shares are changing hands at a price level that yields only two or three per cent on the funds invested in many cases, and the belief is prevalent that capital must become accustomed to a low return. The return to capital is low because the return to labour is low, thus causing idle capital and idle labour.

The view is expressed in high places that greater activity in the home market is desirable, but that if Great Britain is to achieve success she must look to her foreign trade as of old, and not depend upon a prosperity which is based upon "taking in each other's washing."

It is not yet realized that if Great Britain is to increase her foreign trade, she must increase the home power to consume foreign goods. It is not yet realized that British industry is handicapped by too much previous selling abroad under the system of low wages and foreign-investing, and that that method of selling abroad will never become operative again.

[1] The excess of idle funds is due largely to banking policy which is dealt with in Chapter VII.

If a prosperity which is based upon "taking in each other's washing" under free competition, and wages and salaries on a scale to permit what is produced to be consumed with the resulting high productive power matched by a high consuming power and a high standard of living for all, is not attractive to the powers that be in Great Britain, then she is doomed to continue in depression.

Until the people of Great Britain can recognize the logic of exchanging their services with each other on a basis that will permit prosperity for labour and prosperity for capital, under a higher and higher productive power, the need for heavy outlays for doles for both will continue.

It is time the facts were being faced squarely and intelligently utilized. The banks were successful in controlling prices only so long as they could indirectly control wages.

The transcendent economic importance of wages must be recognized if prosperity is to rule in the Machine Age. It should be recognized that the general wage and salary level determines the sterling general price level, and determines the balance between Great Britain's consuming power and her productive power. It should be admitted that a stable buying power of sterling in British markets is ruling because wages are stable and that British prices are low because British wages are low.

The banks lost the power to keep sterling's exchange rates fixed when they lost control of prices. The exchange rate of sterling should rest squarely upon

its buying power in Great Britain, and it should be flexible so as to keep British exports plus incomes from abroad in balance with British imports, without any tariffs, and so as to prevent any harmful effect of prices or wages elsewhere upon the correct sterling price level and upon the British workers' standard of living.

It should be admitted that sterling's exchange rate is fairly steady because wages, and therefore prices, at home and abroad are fairly steady relatively.

For the best interests of Great Britain the buying power of sterling should be stabilized at a level which is fair to debtors and creditors under free competition, and which will bring about the full employment of all the available labour and capital.

Low prices increase the burden of debt, public and private, but, more important, low prices, after higher prices have been ruling, place an unsound burden upon debtors, who are the driving force in commerce and industry, and who are the employers of savings. Prices should be raised so that the burden of servicing the former obligations of debtors will be lightened and so that they will be able to fulfil their vital function in commerce of giving employment to savings, the present glut of which is due to the handicap of low prices.

It is true that a general rise in wages would raise prices, and on first thought it might seem that labour would be no better off after wages were raised than before. But such thinking fails to take into account the effects of an assured consuming power for all that can be produced[1] and the effects

of higher prices upon the doers in commerce and industry, and their ability to give employment to idle capital and labour. Also it fails to take account of the benefits of volume production, the effects of free competition in promoting higher efficiency, the relief from supporting the unemployed, the effect of higher prices upon the burden of the public debt, and the effect of prosperity in affording a wider spread for the tax burden.

The simple requirement for lasting prosperity in Great Britain is *wages and salaries always on a scale that will maintain the general price level of* 1928 *firm under free competition.*

[1]A balance between consuming power and productive power does not mean that there would be a consuming power for all the automobiles, or cabbages, for instance, that could be produced. Naturally there is a limit to the volume of production of each commodity, beyond which production becomes unprofitable. With an assured balance between consuming power and productive power, on the whole, wide-awake capitalists would always give close attention, as they do now, to supply and demand as it affects the opportunity for profits, and they would cease expanding the volume of production of any commodity beyond the point at which profits became unsatisfactory. Recognizing that the wants of man are insatiable, they would turn their attention to the production of, and the creation of a demand for, other commodities. This constant urge to produce something for which there will be a demand is one of the great advantages of economic liberty and the profit motive in making luxuries of yesterday the necessities of to-day with the minimum waste of productive effort.

CHAPTER VI

ECONOMIC POLICIES OF THE U.S. SUBSEQUENT TO THE OUTBREAK OF THE WAR[1]

At the outbreak of the War the industry of the U.S. was disturbed for a few months owing to the uncertainties and changes in international trade resulting from the fact that most of the more developed nations of the earth had suddenly become engaged in trying to destroy each other.

Soon, however, large orders for war materials began pouring into the U.S., and all its production facilities became fully occupied.

Gold Loses Prestige During War.

The credit currency of the Federal Reserve system which had just come into use soon demonstrated its sound worth. Later the U.S., when it became involved in the War, wisely followed the example of Great Britain and cut its currency loose from a fixed parity with gold, causing the Federal Reserve currency to function as a credit currency. The U.S. Treasury, in co-operation with Great Britain and Canada, controlled the dollar exchange rates with other currencies during the War.

During the War wages were raised, which increased the cost of producing goods in terms of dollars, and therefore the purchasing power of the dollar at the close of the War was less than at the beginning.

[1] The readers of this chapter are reminded of the second paragraph in Chapter II.

But as wages in the U.S. had not been increased in the same proportion as they had in Great Britain, the dollar's purchasing power had not lessened as much as the pound's.

Never at any time during the strain of the War did the U.S. credit currency show the slightest fundamental weakness or defect. It answered the needs of the great commercial and industrial activity of the U.S. perfectly.

Prestige Wrongly Restored to Gold after the War.

At the close of the War the currencies of all the more important nations were off the gold standard, and while some nations had but little gold, they felt no special need for it. Gold's value was then much lower relative to the other commodities than it was in the decades preceding the War. The U.S. had plenty of gold, was in a strong financial position, and so had no difficulty in again tying its credit currency to gold at the old parity. The dollar thus restored prestige to gold, and later other nations thought they were giving prestige to their currencies by tying them to gold. *Thus a non-essential commodity was again invested with a fallacious importance—an importance which, as will be shown later, was the primary cause of the War. The reinvestment of gold with this fallacious importance brought civilization to its knees again twelve years after the War.*

Post-war Boom and Depression of 1921.

There was no thought of deflating wages and

commodity prices in the U.S. after the War. Federal Reserve Bank currency and credit were available to commerce and industry at a moderate interest rate. The industry of the U.S. was quickly changed over to peace-time pursuits, which had been curtailed during the War. The demand for many kinds of goods, the production of which had been restricted during the War, was acute, and industry flourished. Workers and commodities were very much in demand. Within twelve months materials in the building trades doubled in price, while wages increased less than 60 per cent. Too great a share of the fruits of industry fell into the hands of profiteers who could not make profitable use of their profits in enterprises giving employment to industry, and so the consuming power fell below productive power, and, as always happens in such circumstances, a violent setback came in 1920. Vast surplus stocks of commodities, reduced production, and unemployment soon became common. Wholesale commodity prices dropped 50 per cent in twelve months' time. However, there was no international stress for gold then or for some years afterwards. Those nations desiring gold "for the purpose of stabilizing their currencies" found no trouble in being accommodated. The U.S. excess of exports over imports had dwindled and continued to dwindle for several years.

Raising Wages Restored Prosperity.

Wages had given way somewhat, and under the conditions prevailing further cuts seemed inevitable.

Many industrialists felt that only by reducing wages could they continue to operate their plants.

Mr. Henry Ford, however, argued that the only way to sell more goods was to increase the purchasing power of consumers, and, as the workers are the backbone of consuming power, he contended that the pay of the workers in such a situation should be increased rather than decreased. Accordingly, he substantially increased the pay of his workers, with the result that other manufacturers employing similar classes of labour had to increase the pay of their more efficient workers in order to avoid labour troubles. When the employers increased the wages of one class of workers, equity demanded that the wages of other classes of workers be increased also, in spite of the unemployment and low profits then prevailing.

The prospect of higher prices, through higher labour costs and greater consuming power, stimulated an urge to spend and invest idle funds ahead of rising prices. Commodity prices were soon restored to a profitable level, and in 1923 wholesale commodity prices reached a level that has not been exceeded since, except for a few months in 1925 and 1926. Prices rose much faster than wages for a time. This did not suit labour and, fortunately for all, labour was fairly successful in its demands for higher wages from time to time, first because of higher prices, and later because of the swollen profits accruing to employers.

In certain industries which had been over-developed during the War, the prices of products did not rise with the general rise in other commodities,

but the cost of living to employees had been considerably increased, and in such industries, by improving methods, ways were found of increasing wages and salaries, thereby keeping the workers in those industries fairly well satisfied.

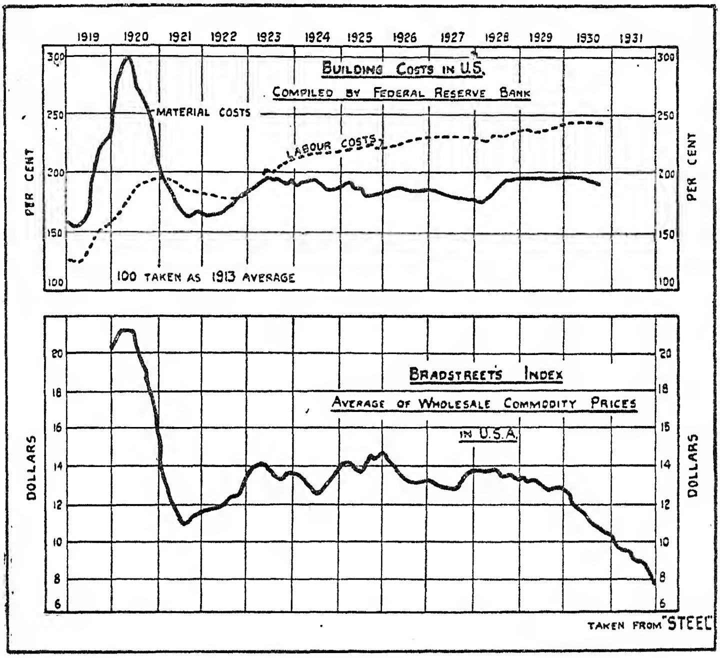

FIG. 1

A temporary reduction in the profits accruing to an industry is often very useful to the standard of living because it stimulates better efficiency in that industry for the purpose of achieving healthier profits.

Fig. 1 shows the material costs and labour costs in building construction, and the average wholesale

commodity prices ruling in the U.S. from 1919 to 1931 —copied from *Steel,* America's magazine of the steel industry.

Statistics reveal that while the wage level gradually and almost continuously rose from the middle of 1922 to 1930, wholesale commodity prices on the whole, with the exception of a few months in 1925 and 1926, receded during the great era of prosperity from 1922 to 1929. The 1920 boom was short-lived because too much of the return from industry passed into the hands of those whose income was out of all proportion to their consuming power. The 1922 to 1929 boom was longer-lived because of the better balance between the consuming power and the productive power, resulting from higher wages as efficiency in production progressed.

In connection with the latter boom it is important to observe that, while wages were increasing and wholesale commodity prices were decreasing, the advantage from volume production and full employment was so great that tremendous profits accrued to capital. The U.S. witnessed a practical demonstration to a moderate degree of what is in store for each nation when it achieves continuous equilibrium between consuming power and productive power.

During the boom in the U.S. it was freely predicted that wages and profits could be limited only by the productive power of the country, and that by increasing the efficiency in production, wages and profits could be correspondingly increased and that prosperity could be made lasting.

U.S. Industry Quite Sound in 1929.

The author contends that the U.S. was in a thoroughly sound position at the beginning of 1929, except for two fundamental defects.

1. The U.S. credit currency was tied to gold.
2. Wages were not high enough.[1]

There was too much inflation in the stock market, but this would not have reached serious proportions had the fundamentals been right.

There was profiteering in the retail trade, and the purchasing power of consumers was being reduced by their interest payments on future-payment purchases without a corresponding increase in the consumption of goods by the moneylenders to whom interest payments accrued, but these defects would have been corrected readily with a little time by healthier competition and better efficiency in retailing, lower prices for cash, etc.

Under the gold standard the international demand for gold and the international demand for the other commodities must be kept equalized in world markets. Owing to the War settlements and the investments which had been made abroad during the preceding years, and due to the fact that the U.S. demanded gold and not foreign goods in the servicing of the international debts owed her, there was an acute demand for gold in 1929 for international interest and debt liquidation payments, which *resulted in lower gold prices of the essential commodities in world markets.*

[1] The bank credit policy of the U.S. was also very faulty. A rational bank credit policy is dealt with in Chapter VII.

If the dollar had been cut loose from gold and allowed its natural exchange rates, U.S. prices would have been free from external depressing influences.

Unfortunately wages were not high enough. *If wages had been higher*, wholesale prices would not have started declining in 1926, consumption would have kept step with production, and there would have been safe employment at home for savings recklessly loaned abroad. Also there would have been sound employment for the savings recklessly employed in the inflation of stock market values. The American people would have been spared the delusion that they could "get rich by selling stocks to one another."

If the U.S. Government had had the vision and the authority in 1927 to announce that it proposed to keep the U.S. power to consume in step with its power to produce by decreeing an all-round rise in wages and salaries from time to time in order to maintain the 1927 general price level firm under free competition, and if it had cut the dollar loose from *artificially fixed* exchange rates and had announced that the Treasury would assume responsibility for the dollar's exchange rates, and that all U.S. exchange transactions must be cleared through the banks designated as its agents and had ensured the *natural* exchange rates for the dollar which would have kept U.S. exports in approximate balance with imports, there would never have been any lull in the prosperity of the United States. The prosperity it was enjoying then would have been a poor imitation of the prosperity and sense of security

it would have been enjoying to-day if the economic benefits to be derived from higher wages had been properly utilized for preserving industrial equilibrium.

Assuming that the 1923 price level was equitable to creditors and debtors, if wages had been sufficiently high through an intelligent plan of regulating wages, and if the U.S. credit currency had been cut loose from gold, wholesale commodity prices could have been held at the 1923 level continuously. This would have brought about more spending and a better balance in the spending and saving throughout the nation, and changes in profits would have been more gradual, reducing the stimulus to violent changes in stock market values. Also, there would have been ample demand for capital for providing better homes and many other facilities for the enjoyment of the workers at home instead of for the enjoyment of workers abroad.

The Federal Reserve bank sought to check the stock market boom, but the damage had already been done. The high rediscount rate resorted to was a deflationary measure pure and simple, and it added to the pressure then active in world markets for lower gold prices of the essential commodities.

Under the influence of the deflationary forces prevailing, industrial corporations could no longer use their handsome surpluses constructively in their own enterprises, and in many cases loaned them out at call on the New York Stock Exchange for the further financing of the stock market boom.

With falling commodity prices and unemployment,

spending fell off further. Then came the stock market debacle in the latter part of 1929. Deflation held full sway, with good credits becoming frozen, bank failures, currency hoarding, serious unemployment, bankruptcy, and despair.

The bankers have been freely blamed for the suffering in the U.S. In the preceding period of prosperity bank deposits grew rapidly. Under the belief then prevailing that prosperity with steady prices would be continuous, the bankers naturally accommodated customers whose ability to repay loans seemed unquestioned. They would have been vigorously criticized had they followed any other policy under the practices then prevailing, but those practices were very faulty, as will be apparent in Chapter VII.

When bankers degenerate into investment brokers and set out to profit through encouraging inflated stock market values and investing abroad for financing producers and consumers abroad instead of those at home they are deserving of all the criticism which has been heaped upon them.

Futility of the U.S. Efforts to Stem Deflation.

The prestige which the U.S. conferred upon gold after the War held the U.S. in depression.

Under the gold standard, deflation could not have stopped before the demand for the essential commodities and the demand for gold were equalized in world markets. If the U.S. had continued the old gold parity of the dollar, and had continued to press for payments in gold in the servicing of the foreign

debts owed her, the demand for gold and the demand for all the other commodities could not have been equalized in world markets, even at a much lower general price level than ruled in the nineties. The misery that would have been visited upon the U.S. in that event may be left to the reader's imagination.

Reckless loaning of government credit can prolong the agony of distressed debtors and embarrassed creditors, but it cannot raise commodity prices in terms of currency tied to gold, so long as an acute international stress for gold prevails, and losses from such loaning would have fallen upon the taxpayers. If wages are not raised, a low rediscount rate for central bank credit or currency tends to lower rather than to raise commodity prices. (More is said about this in Chapter VII.)

In a period of deflation all debtors are inequitably burdened by the greater quantities of goods required to liquidate their debts than were required at the time their debts were contracted.

The tax burden due to public indebtedness, equitable enough when contracted, becomes intolerable under low prices and the reduced industrial and commercial activity over which the tax burden may be spread.

In deflation equity seems to *suggest* lower wages, but the demand for gold under the gold standard *forces* lower wages, or departure from the gold standard if much international trade is permitted. Lower wages reduce the resistance to still lower commodity prices, and in deflation we have lower wages chasing lower commodity prices in a vicious circle.

When there is an acute stress for gold, under the gold standard Mr. Ford's proposal to restore prosperity by raising wages would be futile. Increasing wages in a nation which is on the gold standard increases the gold cost of its products to foreign buyers, and tends to give its currency better purchasing power for competing foreign goods than for the corresponding home-produced goods.

Increasing wages in a gold standard nation not shutting itself off from the rest of the world would, under such conditions, cause gold to flow from it, placing it in the debtor position with all the attendant ills, or force it off the gold standard.

The U.S., with all its vaunted resources in productive facilities and brain power, was held under the heel of gold, an entirely non-essential commodity.

The international demand for gold was due to international debts which involve yearly payments that are really only a small percentage of the yearly incomes of the respective debtor nations. Is not a monetary system which brings about impractical suggestions such as the cancellation of such debts or a change in the gold parity of the various currencies by international agreement, etc., in order to check the havoc from its use in all nations under it, *unworthy of any further confidence*?

Is it not about time we released ourselves from subjugation by our currency, and became its master, so that we may enjoy the fruits of our developments in science and invention and productive efficiency without interruption and turmoil?

In former depressions the U.S. more or less suffered

alone, and deflation proceeded until falling prices brought about more exporting to the more prosperous nations. This of itself was of little importance, considering the vastness of the idle productive capacity of the U.S. in those periods, but the fact that prices had reached a level that was attracting foreign buying, and that a real economic force for checking deflation was manifesting itself, was of vastly more importance. To check deflation and restore prosperity, it is always necessary for a tangible economic force to start operating to arrest falling commodity prices. As soon as it is apparent that such a force is operating, the spending and investing power which has been dammed back by the barrier of falling prices is released, and this, together with the normally produced spending and investing power, has often quickly turned depression into prosperity.

In the present situation all the other nations are in the same predicament as the U.S., and each has placed a tariff wall around itself so as to prevent the loss of much of its own spending power to the U.S. Furthermore, in all depressions prior to the War, the U.S. was a debtor to Great Britain, a free trade nation, which made it easy for the U.S. to sell to Great Britain whenever prices in the U.S. dropped materially. In the present depression conditions are quite changed. The U.S. has become a creditor nation, and there is now no free trade nation to check the falling gold prices of U.S. goods. If any world prosperity is to be brought about, the U.S. must prepare herself to rise from depression under the condition of adverse balances in the international

trade of goods and services and spending abroad, or lose part of her foreign investments.

The U.S. must remember that her previous era of prosperity was due to the unusual degree of balance maintained between her power to consume and her power to produce, and that *that balance resulted from raising wages as efficiency in production improved.* The U.S. must now enable forces entirely within herself to function in casting off depression, and under industrialization must realize the dominating importance of the economic forces involved by changes in wages.

President Roosevelt's Policies.

President Roosevelt took office in the midst of a crisis of the depression. It was apparent that the old way of allowing depressions to run their course under the gold standard would mean disaster under the conditions then ruling. The President, therefore, very wisely, quickly cut the dollar loose from gold, in order to avoid a complete collapse.

Enjoying the confidence of the people in his courage and sense of honour and fair dealing, he was soon empowered through the National Industrial Recovery Act to exercise control over the currency and industry of the U.S. Since then he has not hesitated to do whatever in his judgment held a promise of improvement.

He achieved a rise in prices through threats of inflation, more government spending, shorter working hours, and government control of industry. But are these sound measures?

Inflation, if embarked upon, would result in a stampede to convert funds and fixed-interest securities into goods and property, and prices would rise. The danger of such a policy is that no convenient stopping place would be likely to manifest itself while the value of money remained above the cost of printing it.

Shorter working hours would distribute the present work among more workers and reduce the number of the totally unemployed by increasing the number of partially employed. If the hours of the workers are shortened the workers must produce less. If they produce less they must consume less. Is there a worker anywhere who wishes to produce less with a corresponding reduction in his consuming power? Workers should not be asked to produce less while their desire for higher standards of living remains unsatisfied. The fact that there is now an over-supply of workers is not the cause of the depression, and reducing the consuming power of the workers employed is not the cure.

The government control of industry with a view to controlling output and prices, is to thwart the operation of the laws of supply and demand and the survival of the fittest, and leads into deeper and deeper water, and the seeming need for many more complicated government responsibilities.

Government interference with the laws of supply and demand and the survival of the fittest results in attempts to keep alive the high cost producers in industry to the disadvantage of the low cost producers. If President Roosevelt's "new deal for the

forgotten man" is to deteriorate into a plan which will cause hand-labour to compete again with the machine, and which will force the well-equipped producer to operate at part capacity, it will deteriorate into a plan which will cause precarious livings to be eked out by inefficient methods and the people of the U.S. will be disappointed. Prosperity means high standards of living. High standards of living are possible only through volume production and the correct distribution of the return from industry between the savers and spenders.

Back to the land is the last resort of many unemployed who prefer to eke out an existence by their own productive efforts rather than be dependent upon charity to prevent starvation. Thus when times are bad there is an extra supply of workers trying to make a living on the farms,[1] and an over-supply of farm products at low prices is an inevitable result. A subsistence living on the land is not the cure for the unemployment problem, and there will be no real prosperity while workers have to resort to such a standard of living.

That "the buying power of the *farm population* must be raised relative to that of the urban population" is clap-trap. The present farm problem will be solved only by a demand in the other industries for workers now on the land. Only by *reducing* the population on the farms will the standard of living on the farms be raised.

[1] In times of depression the farm problem is also aggravated by the position of the farmers who are in debt. Their only hope of paying off their mortgages lies in increasing their production. Other factors bearing upon the standard of living on the farms are mentioned in Chapter I.

Those eking out livings on the land are in the same position economically as those eking out livings in other ways. The solution of the problem of all those unfortunates is the same, i.e. a balance between consuming power and productive power that will result in a healthy demand for labour.

It must be remembered that farming is only one of the many U.S. industries. The correct equilibrium between the farming and the other industries of the U.S. can be achieved only through a free and orderly operation of the law of supply and demand. There is nothing sacred about the farming industry. Hosts of workers left the farms during the era of prosperity between 1922 and 1929, and reluctantly returned again after the balance between consuming power and productive power became seriously disturbed in 1929. They will leave the farms again to enjoy a much higher standard of living in the other industries as soon as a move is made to ensure a balance between the consuming power and productive power of the country as a whole. A reduction in the number of those seeking a living on the farms will bring a much higher standard of living to those who remain and work the more productive lands and use more efficient methods.

Under a free operation of supply and demand, and with a balance between consuming power and productive power in the country as a whole achieved through higher pay for employees, the standard of living in the farming industry will quickly approximate the standard of living in the other industries. The standard of living of the workers in the other

industries would quickly set the standard of the workers in the farming industry, regardless of whether the latter were land owners, renters, or farm hands.

The Government has a most important obligation to commerce and industry, but it should be discharged in a way that will permit the laws of supply and demand and the survival of the fittest to operate freely in bringing higher and higher standards of living to all.

The President has advocated increases in wages, but apparently he lacks a full appreciation of the transcendent economic advantages to all from decreeing rises in the general wage and salary level for bringing consuming power into step with productive power, and for maintaining that desirable condition.

Price Fixing and Government Spending in the U.S.

The activities of the N.R.A. consisted in a system of price-fixing, government loaning to distressed industries, and government spending for projects which, in the main, are non-productive. Mr. J. M. Keynes has advocated lavish government spending as a means for restoring prosperity, but, economically, such spending constitutes nothing more or less in the main than *a dole at high wages and salaries* to many who would otherwise be listed as unemployed.

Why waste capital in unnecessary government projects, and thus increase the burden of public debt which is already much too heavy?

Some think prosperity could be achieved by injecting more money into the system. They would have the Federal Reserve Banks purchase securities in the

open market, but that procedure would only add to the present glut of unemployed capital. The new money thus created would fall into the hands of savers and would thus be available for investment in productive enterprises mainly, but the incentive for such investment will be lacking while there is insufficient consuming power for products of present productive enterprises. More is said about this method of achieving prosperity in Chapter VII.

No matter how they are started, more buying and greater industrial activity cannot be maintained for any length of time without much higher wages and salaries for the consuming masses under free competition. To try to prime the pump for more spending by any means other than the assured prospect of the *direct* means—higher prices through higher wages and salaries—can result only in piling up unnecessary handicaps for the future.

Useful employment for all in the Machine Age is impossible without a natural attraction between idle capital and idle labour, and a natural attraction between idle labour and idle capital is impossible without free competition.

If free competition were to be established now without the assurance that wages would be materially raised in the near future, *prices would fall*, as they always do under free competition when productive capacity exceeds consuming capacity, and another crisis would soon be precipitated. Heretofore the *artificial* link of the dollar to gold prevented prices from falling below a level that attracted foreign buying. In the present situation, the gold standard has been so

wrecked, and the need by other nations of conserving their buying power for their own goods is so acute, that no matter how high the price of gold or the price of silver is set in terms of dollars, other nations would protect themselves against such practices, and the U.S. would gain little, if any, assistance in stemming the downward tendency in prices and the resulting despair.

This time the U.S. must depend upon its own resources for matching its power to produce and its power to consume. The depression was caused by the fact that wages and salaries were not high enough in 1929, and *the only way out of the depression is to treat the cause.* By raising wages and salaries under the plan suggested in Chapters I, II, and III, employers would not be embarrassed in the least, and would gain quite as much in proportion as wage and salary earners in the end, and more in the beginning.

Unfortunately the present U.S. "dole" is being paid in the main out of borrowings instead of out of income, and a debt is piling up which must be paid by producers later, and which will correspondingly reduce their consuming power later. The "dole" is so large that to pay it out of taxes would be practically impossible. Even though such outgo were fully covered by current income, the consuming power of the employed and the capitalists, especially the smaller capitalists, would be materially reduced by the taxes paid. Furthermore, the taxes paid by those having larger incomes would reduce the capital which has been saved and which should be available for

providing more efficient means of production and raising the standard of living of the American people instead of providing a "dole" for them.

The unemployed and those on the government "dole" should be producing the goods and services they now so urgently desire, and they would be producing them under the correct economy for the Machine Age, which would treat the cause of the trouble out in the open where all could comprehend the end desired and the soundness of the means used for achieving it.

The old system of haphazard wage adjustments with a constant conflict of interests and turmoil must give way to a system that will permit the maximum possible return to both labour and capital, and thus render their interests mutual.

The N.R.A. activities amounted in the main to a copy of what Great Britain has been doing for the past twelve years, and they constitute an economy which will hold the U.S. firmly in depression. The U.S. Government has been more lavish in spending borrowed money, but giving employment to capital in that fashion cannot last, even though the tax rates in the U.S. are still lower than in Great Britain.

Control of Purchasing Power of Currency Unit a Government Responsibility.

The President should realize that the control of the purchasing power of the currency is a most important government responsibility. The President recognized this in his famous announcement regarding his aim to restore prices and stabilize the

purchasing power of the dollar. Not only does equity to the payers of the public debt, and equity between all debtors, who are the originators and doers in commerce and industry, and their creditors, depend upon the correct control of the purchasing power of the dollar, but the balance between the power to consume and the power to produce also depends upon the correct control of the purchasing power of the dollar.

If the President would realize that the general wage and salary level is the all-important factor in determining the general price level, and do only what he said he would do for the dollar *by the only possible sound means*, the "new deal for the forgotten man," and a very good deal for him, too, would follow automatically.

The President should stop the serious conflict of interests between the capitalists themselves and between capital and labour brought about by the activities of the N.R.A. He should confine his efforts for relieving the depression solely to the control of the purchasing power of the dollar, a purely governmental responsibility. He should go straight for the objective, by announcing that he proposed to have rising wages and rising prices follow each other for a time until former prices were restored, and all the U.S. labour and capital became comfortably employed again, and that he proposed that thereafter the purchasing power of the dollar would be pegged for all time at the price level then ruling.

Under this programme, as volume production and better efficiency tended to reduce the cost of goods,

higher wages and salaries would be required from time to time in order to keep the general price level in terms of dollars up to the level adopted as the standard, and thus increases in consuming power would match increases in production—equilibrium between consumption and production would be automatic. With such an announcement by the President, the soundness and justice of his programme would soon be understood. Industry and commerce would then have something definite upon which to base plans. *Uncertainty about the future would give way to certainty.*

It would soon be realized that the new general price level could be depended upon never to recede and that deflation was a pestilence of the past. Also it would soon be realized that the interests of labour and capital had been rendered mutual in fact as well as in theory, and that under the plan announced each would constantly receive the maximum possible return compatible with a balance between consumption and production and the comfortable employment of both.

The advantages of volume production would permit ample profits under higher steady prices and a much higher general wage and salary level.

In an over-developed industry rises in wages would not necessarily cause a corresponding rise in the prices of the products of that industry under free competition. This would prove potent in eliminating high cost producers. The best interests of all concerned, including the high cost producers themselves, demand that no business should be allowed

to live which cannot pay wages and salaries on a scale that will permit what is produced to be consumed.

It must be remembered that the law of the survival of the fittest operates somewhat differently in prosperity than it does in depression. While the survival of the fittest was allowed fairly free rein during the period of prosperity in the U.S. between 1923 and 1929, in general its operation proved beneficial to the high cost producers. Many of the less efficient producers became better equipped and more efficient. Others were taken over by more efficient concerns upon mutually satisfactory terms. Many small concerns were closed down, not so much because of reduced profits, but because there was a steady demand for workers in the efficient concerns at high wages and salaries, in spite of the great progress in labour saving. The owners of small concerns and businesses found higher remuneration as employees of large efficient concerns than as owners of small inefficient concerns.

The "Money Changers."

In his inaugural address, President Roosevelt cast reflection upon the "money changers," yet he allowed the international money changers free rein in their play with the exchange rate of the dollar. The conduct of international exchange is a government responsibility. A government should be master of the exchange rate of its currency for its foreign trade in goods and services. In the main, it should limit the exchange transactions in its currency within the

nation's confines to those involved by its exports and imports in goods and services.

The foreign buying power of any nation's currency unit should rest solely upon the currency unit's buying power for goods at home. The currency unit's exchange rate should be adjustable so as to take care of variations in its buying power relative to that of other currencies for the purpose of keeping the nation's exports in goods and services in approximate balance with its imports.

For a nation to attempt to lessen its currency unit's buying power abroad by any means other than lessening its buying power at home, that is without raising prices at home, would tend to increase its exports and lessen its imports. Any advantages to the U.S. from pursuing that policy would be gained to the disadvantage of other nations, and at best could be only temporary, and would prove harmful later.

Furthermore, the U.S. is a creditor nation, and if it has any concern about payments on its foreign debts, the exchange rate of the dollar should be set so that U.S. imports will exceed exports.

The way a nation has allowed funds to be transferred to and from it through exchange to accommodate the operations of international speculators, and thus disturb the *natural* exchange rate, which normally should result only from the nation's international trade in goods and services, will cause astonishment in the future.

President Roosevelt Decided to Buy Gold.

In November, 1932, President Roosevelt announced

that the U.S. Government would buy gold in world markets in the hope of raising the general price level in terms of dollars.

With freedom for the movement of goods from one nation to another, and with a number of the other important currencies tied *fixedly* to gold, the U.S., by lowering the gold value of the dollar, could cause U.S. goods to move into foreign markets for a time, and this could be instrumental in starting a period of higher dollar prices. But with neither of these conditions obtaining, paying fancy dollar prices for gold could have but little more basic effect upon the general price level in the U.S. than would paying fancy prices for Napoleon's ashes or some other non-essential commodity which is not freely produced and freely consumed. The gold-producing industry of the U.S. is nil compared with all other industry, and while prosperity for the gold producers and the gold fetishism last, lasting prosperity for the other industries is impossible.

The U.S. must realize that cheapening its currency in terms of gold is a game which a number of other nations are now free to play also, and the value which gold may attain in terms of the leading currencies of the world now depends solely upon the attitude of the players of the game.

The supply of gold is very limited, and if a spirit of rivalry prevails to a sufficient extent, the value of gold relative to the other commodities can be pushed very much higher than its present value. On the other hand, if sanity prevails, and the futility of the use of gold as an international measure of

value is recognized, all the leading governments will also recognize that buying and stocking gold is just as absurd as would be buying and stocking any other non-essential commodity having an artificially created monopoly value which can be quickly lost.

Professor Irving Fisher, who has attracted much attention by his "Market Basket" dollar and "Commodity" dollar, or a dollar of constant purchasing power, is considered by many as the author of President Roosevelt's plan for manipulating the gold parity of the dollar.

In the future it will be wondered how Professor Fisher, and the many others who have devoted so much time to theorizing about economic phenomena, could see the virtue of a currency unit of constant purchasing power, and yet entirely overlook the only means by which such a currency unit is possible. How different would be our present situation had they pondered more over causes rather than trying to conjure with what should be effects. If they had built upon a solid foundation by making proper use of the simple fact that raising or lowering wages will raise or lower prices, and if they had recognized that the wages and salaries paid in any nation determine the balance between its power to produce and its power to consume, and if they had recognized that each nation must be satisfied to allow imports to balance its exports, the world would have been spared its present suffering.

The U.S. has become industrialized to such an extent that capacity production and full employment can be achieved only by much more spending.

Sufficient spending will not be brought about by any measure which does not deal directly with the basic cause of the present trouble—*wages and salaries were not high enough in* 1929.

To try to bring about prosperity *by any means* that does not start with the prospect of much greater consuming power for consumers' goods is to attempt to put the cart before the horse. When more buying power for consumers' goods is in sight, more employment for capital and labour in the production of capital goods will be in sight.

In the previous period of prosperity surplus profits were invested in capital goods to such an extent that more consumers' goods came into the market than there was consuming power for. Smaller profits than in the previous period are inevitable for a time in any case. Shall they continue doubtful and inadequate, or shall they be more certain, but a little less excessive than in the previous period, through a consuming power in step with productive power?

In those industries which are especially suffering from over-development, under-consumption, and low prices, it must be realized that the only hope for them lies in bringing about a greater consuming power for the consuming masses. This is possible only through a higher general wage and salary level, and the logic must be seen of raising wages in such industries as well as in all other industries.

The U.S. Government Buys Silver.

In the summer of 1934, the U.S. Government launched a silver-buying campaign, and offered a

higher price for silver in terms of U.S. dollars. While paying higher prices for gold had had little effect in raising U.S. prices, the silver producers, or at least the politicians of the silver producing States, were successful in persuading Congress that paying higher prices for silver might do the trick.

The effect of the U.S. paying higher prices for silver was mainly to raise the world price of silver and enable the producers and hoarders of silver to get more gold or other commodities in exchange for silver. The effect upon commodity prices was the same as the effect of paying higher prices for gold.

The higher prices paid for domestically produced silver amount to a subsidy to the silver producers of the U.S. and is on a par with the subsidies paid in other U.S. industries.

The countries in which the silver fetish ruled commenced to lose their silver, and the effect upon them was exactly the same as the effect in gold standard countries when the world price of gold is raised. They were afflicted by deflation and were forced to devalue their currencies in terms of silver to prevent disaster.

The experience of the U.S. in bidding up the prices of silver is just another example of the utter futility of one nation trying to accomplish something beneficial for itself through measures harmful to other nations.

Fortunately all the nations are fast learning the fallacy of reverence for inflexible exchange rates, and the folly of binding themselves to any *fixed* parity of their respective currency units.

The Objectors to the "New Deal."

There are many objectors to the "New Deal" and there is much talk about "the American Tradition," "Back to Liberalism," "the need for free competition," "economic liberty," etc. Certainly economic liberty has been a fundamental of the American tradition. Also a fair balance between the home consuming power and productive power has been traditional in America. The two together are a wonderful combination. Before much progress can be made, however, in overcoming the depression the supreme importance of the latter must be recognized.

Those objecting to the "New Deal" generally confine their recommendations to one or more of the following: enforce free competition, allow prices to fall, reduce Government spending, balance the budget, permanently fix the gold parity of the dollar.

As long as there is a disequilibrium between consuming power and productive power, depression will continue. To resume free competition under that condition would be to start again the vicious circle of lower prices, lower production, and lower employment, and serious distress for debtors private and public.

Those advocating lower prices are confined mainly to those who think they have fixed incomes. If prices went as low as they would be likely to under free competition and under the present disequilibrium between consuming power and productive power, many of them would find that their fixed incomes were not nearly so fixed as they had supposed. Certainly debtors, who are the mainspring

of commerce and industry, would not welcome lower prices, and not many creditors are so short-sighted as to wish to take chances on having the position of their debtors impaired through lower prices.

Government spending is one way to raise consuming power. To reduce Government spending in the present situation would increase the disequilibrium between consuming power and productive power, and thus increase unemployment.

There is no argument for unbalanced budgets. Budgets should always be balanced, but to achieve a balanced budget when consuming power is so fundamentally out of step with productive power is a problem which should be solved by first achieving equilibrium between consuming power and productive power.

For anyone to advocate permanently fixing the gold parity of the dollar is an admission on his part that he has failed to recognize the gold standard as the great barrier to any enduring prosperity and world peace (for more about this see Chapter XI) and that he has failed to recognize the impracticability of getting other nations to bind themselves to similar fixed gold parities for their currency units.

All those things which are objected to in the "New Deal" are the result of trying to treat effects and not the cause of the depression, and changes now being prescribed would only treat the effects of treating effects and not the cause of the disequilibrium.

Consumption should be kept in step with production. The untold possibilities of the Machine Age should be enjoyed to the full. Everyone should be

ensured a standard of living in keeping with his ability and desire to produce. The Government has most important obligations, and to fulfil them it should be charged with responsibility for the following—

(*a*) Maintaining the internal buying power of the dollar at the 1928 level *by the only possible means* —control of the general wage and salary level. The "dispute method" of adjusting wages is far too crude for the needs of the Machine Age.

(*b*) Regulating the exchange rates of the currency unit so that exports plus foreign incomes will be kept in balance with imports under free trade.

(*c*) Enforcing free competition, which is the life of trade, and,

(*d*) Paying old age and disability pensions through a small tax on all pay rolls.

With economic liberty ruling subject to the Government fulfilling its above logical obligations all need for the numberless unsound interferences with commerce and industry which seem necessary under the present hodge-podge economy would then quickly disappear.

Wages and salaries always on a scale that will maintain the 1928 *general price level firm under free competition is the simple requirement for lasting prosperity.*

If the President and his associates could become interested in treating the cause of the depression and ask Congress to consider—

Firstly, the abolishment of the "dispute method" of adjusting wages;

Secondly, the control of the buying power of the dollar, under free competition, through the business-like control of the general wage and salary level; and

Thirdly, a common-sense management of the exchange rates of the dollar,

then no matter how quickly Congress responded, prices would harden before it could act, and the idea that the U.S. can produce more than she can consume would soon give way to the idea that no country can ever produce by the most efficient organization possible the equivalent of more than its people would like to produce and consume.

A surplus of workers and a surplus of goods is a thoroughly unnatural and artificial condition which has been brought about by the practice of a fallacious economy. By enforcing free competition—ensuring economic liberty—and providing a dollar of constant purchasing power at the right level, *by the only possible means*, a shortage of workers and a shortage of goods would become chronic.[1] In view of man's desire for a higher and higher standard of living this is a natural condition that should be constantly ruling.

[1] Under the correct economy "buyers' markets" would give way to "sellers' markets" with the result that the need for high powered salesmanship would be reduced with advantage to producers as well as consumers.

CHAPTER VII

BANK CREDIT: ITS USE AND CONTROL

The previous chapters have been devoted largely to pointing out that the buying power of money, other conditions being equal, is determined by wages—*that the wage level is the natural regulator of the price level.* Also it has been pointed out that for the best interests of both capital and labour wages should always be raised when the general price level tends to fall below the level adopted as the standard, and that no rises in wages should be allowed when the price level is tending to rise above the level accepted as the standard, the object being to ensure a steady general price level—a steady buying power of the currency unit—which, at the right level under free competition, would ensure constant balance between consuming power and productive power.

When consuming power is out of balance with productive power a glut of money can be available to investors with a very little or a very slow effect upon prices, but with balance, more money and bank credit in the hands of spenders and investors than is necessary for the comfortable employment of all the available labour will cause prices to rise. When consuming power is in step with productive power, prices could be maintained by unsound banking practices above the level accepted as the standard for a long period, and thus with prices rising and wages and salaries remaining stationary, workers

and savers could be more or less defrauded over a long period. For this reason, and for the reason that various proposals have been made for the control of bank credit having as their object the restoration of prosperity, it seems desirable to consider briefly how money originates, and to point out what changes, if any, should be made in present banking practices to ensure the continuous well-being of all concerned.

In this chapter no consideration is given to the effects of international trade upon prices, as the internal price level would be entirely independent of price levels abroad under a rational exchange policy which is dealt with in Chapters VIII and IX.

It is important to realize that currency is not really capital. Currency is a receipt or an order for capital, just as a bank cheque is an order for currency. Currency and credit are the vehicles by which capital becomes liquid and can move about in performing service in commerce and industry. A high charge for this medium, if persisted in, creates a vicious circle which will bring unemployment and poverty to the proudest nation, on the gold standard or off.

Gold is a very expensive medium or vehicle for the movement of capital, and on account of its cost capital has been deprived of much of its potency in the past. If it had been necessary for each promise to pay to be engraved upon a commodity of corresponding intrinsic value, capital would have been deprived of much more of its potency in the past.

The interest rate for the use of capital should be governed normally by the law of supply and demand. In the best interests of all concerned, the charge

for the use of the medium by which capital functions in commerce and industry should be kept reduced almost to the bare cost of providing the useful medium.

Credit the Life Blood of Commerce and Industry.

If the modern bank-note currency were completely freed from any connection with gold, as it was during the War, and if the general price level were maintained stable by the Government control of the general wage and salary level, it would be found that the expansion and contraction of credit by bankers to suit the needs of commerce and industry, and the present relation of the bankers to the central bank, have possibilities of affording the ideal monetary system for an industrialized age.

As a simple example of the part credit plays in keeping the wheels of commerce turning, and the way it becomes the basis of modern currency, we might take the case of a truck-maker who requires £500 worth of steel to finish a contract for trucks he has in hand. Not having the ready money, he might give his promissory note for £500 to the steel-maker, payable in sixty days. The steel-maker could endorse the note and pass it on to a coke-maker in payment for coke required in producing steel, and likewise the coke-maker could pass the note on to the coal-miner, for the coal required in making his coke, and he in turn could pass the note back to its original maker in payment for trucks. After the truck-maker had discharged his obligation by the sale of trucks to the coal-miner, he would naturally destroy the note.

Thus the truck-maker's promise to pay money, secured by his ability to produce goods for which there was a demand, could pass from hand to hand in payment for goods, the effect being much the same as if currency had been used. No bank has been involved in this example, and the purchasing power of currency has not been affected in the least. The circle of exchanges of goods has been carried through without the aid of legal-tender money.

While privately executed negotiable notes may be passed in commerce almost as currency, their use in practice is very much restricted because the ability of the maker to pay cannot be known by everyone to whom the note might be offered.

The Services of the Banker.

The use of a promissory note for making payments in commerce is sound in principle, and only requires the services of the banker to make it thoroughly practicable. If the truck-maker, instead of making his note payable to the steel-maker, had made it payable to his banker, pledging the trucks he was building as security, the banker would have given him bank credit, and credited him with a deposit equal to the face value of his note. Then the truck-maker would have paid the steel-maker by a bank cheque, and in turn the payments by the steel-maker, the coke-maker, and the coal-miner would have all been made by bank cheques. If the truck-maker used the cheque he received from the coal-miner for paying off his loan from the banker, the latter would return to him his note, which he would destroy as in the first case.

Not the slightest harm would result from this destruction of the note, or the reduction of the outstanding bank credit, because if the truck-maker or any of the other producers in the example taken required similar accommodation at any time, the banker would normally be only too pleased to accommodate them. To those who complain of the power possessed by the banker of making and destroying credit, it may be pointed out that the original maker of the note, not the banker, created the credit, and that he likewise destroyed the credit.

It will be noted in the example cited that while the banker probably had plenty of currency on hand, and could have made the payment to the truck-maker in currency, no currency was used. If the truck-maker, steel-maker, coke-maker, and the coal-miner had all used the same bank, the bank's deposits would not have been changed by the circle of transactions. As the deposit of one of the parties was depleted, the deposit of another would be increased. When the banker credited the truck-maker with his deposit, the banker's liabilities and assets were increased by the same amount. When the note was paid the banker's liabilities and assets were both reduced by the same amount without the least harm to anyone. In this way bankers build up or reduce the bank credit extended to commerce and industry.

Generally speaking every loan a bank makes which is not a renewal of a previous loan increases its deposits, or those of other banks. The same is true of any purchase a bank may make, such as the purchase of government, or other, bonds, etc., as long as

the purchases are from the public and not merely transfers from one bank to another. Bankers, of course, must always fortify themselves with a reasonable surplus of cash or quick assets, which are known as the banks' reserves, for meeting an excess of withdrawals over new deposits.

If the steel-maker who was paid with a cheque by the truck-maker deposited that cheque in another bank, the deposits of the truck-maker's banker would be reduced by the amount of the cheque, but normally this would be offset by cheques on other banks being deposited with him.

The Function of the Central Bank.

If, however, the deposits of a banker were materially reduced by his depositors' cheques being paid into other banks, the banker would find himself owing other banks. To keep himself solvent and in a position readily to meet such obligations he might do several things—

(*a*) He might pay the bank or banks he owed from his reserves—his cash or deposits in other banks. To carry this far would, of course, reduce his reserves, against which other loans could be made, as banking practice requires that the banker have a certain ratio of reserves to deposits in order that he may further expand his bank credit.

(*b*) He might endorse some of the promissory notes he held and transfer them to the banker, or bankers, whom he owed. This is often done, good promissory notes or bills of exchange, their equivalent, passing from one bank to another almost in the same way

as legal tender. In this case the banker transferring the notes would lose a good part or all of the subsequent interest income on the notes transferred. Also he might transfer bonds, or other instruments of debt, to the banks he owed. In this event he would also lose the interest on the unexpired terms of the instruments transferred, which as a rule would be lower than the rate he expected to charge for new loans.

(*c*) He might use the facilities of the central bank, and here is where the central bank comes into the picture. The banker might transfer some of the notes or bills of exchange he was holding, which were eligible, to the central bank, the banker endorsing them and guaranteeing their payment to the central bank, and getting for them central bank credit or new central bank currency. The banker then could draw on the central bank credit or currency thus created, for paying the other banker or bankers whom he owed.[1] If the central bank rediscount rate were 2 per cent and the obligations transferred were bearing 6 per cent interest, the banker would get the difference of 4 per cent for the unexpired terms. When the obligations taken over by the central bank matured, the original debtors would pay the central bank in currency, or central bank credit received in payment for the goods which secured their obligations. Naturally, when the original debtors liquidated their

[1] In Great Britain most of the rediscounting is done through bill brokers and discounting houses, and when money is plentiful the facilities of the central bank are little used, but the effect is practically the same, and for the purposes of our discussion it may be assumed that all rediscounting is done directly with the central bank. Much of the discounting in London is done in connection with international transactions. This phase is dealt with in Chapters VIII and IX.

obligations, their notes would be destroyed, and the currency or central bank credit received by the central bank in their liquidations would also be destroyed. Again, the original debtors of the obligations created the credit and destroyed the credit or currency involved by the use of their notes or bills of exchange. By the use of the credit of the original makers of notes and acceptors of bills, through the services given by the banker and the central bank, commerce and industry are accommodated with the currency and bank credit which enable goods and services to be produced and distributed.

The Use of Bank Credit.

If the banker in our illustration had sent some more of the eligible obligations he was holding to the central bank for rediscounting, he could have further increased his reserves of central bank credit and currency, and thus placed himself in a position to loan safely more bank credit to other borrowers.

In our illustration of the transactions of the truck maker, steel maker, etc., the loan was made for the purpose of enabling the truck maker to get the steel necessary for the completion of a contract which he held for a certain number of trucks, and when the trucks were completed and sold the loan was liquidated from the proceeds of the sale, and therefore the accommodation was required for a short-term loan.

Short-term loans are also made to pay wages while goods are in process of manufacture and are liquidated when the goods are made and sold. Long-term loans

may be made for building, factory extensions, public improvements, etc., which are soon completed with the labour and materials available at the time, but the loans which make expenditure for such work possible may not be liquidated for a number of years after the work is completed.

If there is to be employment for all the available labour there must be a demand for labour in the projects requiring long-term loans as well as in the productive pursuits which can be financed by short-term loans.

There would be no danger of a disequilibrium between the labour available for production and the money being presented in demand for goods and services if all loans were short-term loans, because the money for the liquidation of a short-term loan is being taken out of industry's yield practically while the money loaned is being spent. In the case of long-term loans, however, the money for liquidation is taken from industry's yield over a long period after the money loaned is spent.

All loans to industry are made only for money which will be used promptly in paying for goods and services, and if long-term loans are made too freely more goods and services may be demanded than the available labour can supply.

When all the available labour is fully employed consuming power is high, and labour and all kinds of goods are in demand. Under such circumstances producers in industry find many opportunities for increasing their profits if they can finance an increase in their productive power, and bank loans are

therefore very much in demand. If long-term loans are made by expanding bank-credit too freely and not from savings, claims may be presented in demand for goods and services faster than the labour and facilities available at the time can supply them. In that event prices will rise—prices for the goods and services which are available come into equilibrium with the greater volume of claims being presented for them.

Without interference by a monetary authority the banker could continue to expand his bank credit and charge a comparatively low rate of interest. As the cost of manufacturing bank credit is very small a banker can continue to loan to credit-worthy borrowers with safety almost indefinitely. The main requirement for safety to the banker and the borrower is that prices will not fall before the loan is liquidated. The more prices rise the easier it is to liquidate loans, and therefore the more freely loans are increased the easier becomes the liquidation of previous loans.

The rapidity with which prices rise in a wave of inflation depends largely upon the rapidity with which wages are raised. If wages were raised with rises in prices, a wave of credit inflation would continue, if not interfered with by a monetary authority, until prices reached fantastic heights.

On the other hand, if wages were held stationary because of the fact that prices were higher than the level accepted as the standard,[1] prices would not rise nearly so fast or so far as they would if rises in wages

[1] In previous chapters it has been pointed out that in a rational economy when labour is comfortably employed, wages should not be raised when prices are tending to rise. Wages should be raised only if there is an indication that prices will fall if wages are not raised.

were allowed with the higher prices and scarcity of labour. If bank credit were made cheap for long-term loans, inflation could proceed a long way, however, under steady wages. The reaction, or the wave of deflation, when it finally came, would soon be stopped if rises in wages were made as soon as prices fell to the level accepted as the standard.

Normally when labour is not fully employed there would be no inflationary tendency from the expansion of low interest bank-credit to accommodate credit-worthy borrowers with long-term loans while material unemployment continued. However, when depression rules a surplus of savings becomes available for long-term loans, and the trouble is that they fail to find employment because the doers in industry are unable to use them with profit. In such periods there is insufficient consuming power to provide profitable employment to the existing facilities of production and prices are low. Low prices are the great barrier to the employment of savings, and, as is pointed out in previous chapters, since wages determine consuming power and prices, the only sound correction is to be achieved by a general rise in wages and salaries.

When the banks are expanding bank credit in a wave of credit inflation at a moderate rate of interest for loans, real savings receive only the same interest rate as the bank credit which is occupying the field in competition with real savings. Thus the interest rate for savings is not in harmony with supply and demand for savings, and sound economic principles are being violated.

Fundamentally, capital is only stored labour, and the *entrepreneur*[1] generally can choose between employing labour and employing capital in the form of plant and machinery to perform his tasks. Labour can be displaced by employing invested capital,[2] and existing invested capital can be displaced by investing savings. Generally speaking, the yield from industry is divided between wages for labour, profits for invested capital, and interest for savings, and if sound economic principles are ruling, labour, invested capital, and savings are in competition with each other for their respective shares of the yield.

If, when labour is fully employed, the relative earnings of labour, invested capital, and savings are not in harmony on the whole with their relative replacement values in industry, it signifies that sound economic principles are being violated. Based upon sound economic principles some interest is being cheated.[3]

If wages are low the lion's share may go to profits and interest. If prices rise a smaller part of industry's yield is required to pay interest, and if prices fall the part required to pay interest may leave a very small part for profits. In any event the amount industry can yield is limited, and if some claimants take more than their share others must take less.

[1] In the discussion which follows, the reward of the *entrepreneur* is assumed to be included in the reward to labour.

[2] By "invested capital" is meant the part of invested capital which is not paying interest or rent to a lender or lessor, and by interest is meant interest or rent being paid to a lender or lessor. The distinction may not be in strict accord with strict orthodox usage, but will suffice for what follows.

[3] By "sound economic principles" and the "sound allocations" to wages, profits, and interest, in what follows, is meant what is implied in this paragraph.

A distribution of industry's yield which will keep labour, invested capital, and savings fully employed is always possible, but unfortunately in adjusting the relative allocations of the yield from industry to the several claimants the human element is involved, and the rule of sound economic principles may be very easily thwarted by wrong artificial measures.

In any physical problem where equilibrium is desired between opposing forces which are all variables, it is *always necessary first* to evolve an unvarying unit of measure which is suitable for valuing and adjusting the forces involved.

Without attacking in a similar way the problem of allocating the money yield of industry to the several claimants in harmony with sound economic principles, any satisfactory solution is beyond the power of human intelligence.

Fortunately, however, we have the essentials at hand which will provide the necessary unvarying unit for measuring the earnings of labour, invested capital, and savings, and which will provide the basis upon which the relative allocations should be made, so clearly and obviously, that no producer who will reflect upon them can question, or want to question, their fairness to all and their accord with sound economic principles.

In the economic realm a currency unit of unvarying value[1] is of vital importance if any rationality is to

[1] The gold standard has to be eliminated from consideration because, as is explained in previous chapters and particularly in Chapter XI, the conditions favourable to its operation have passed. Also as a standard of value of any stability gold failed signally and was constantly interfering with the rule of sound economic principles, even when the conditions most favourable to the operation of the gold standard prevailed. As a

rule in making the relative allocations to the several claimants of industry's yield.

As previously pointed out, *wages are the natural regulator of the buying power of the currency unit*, therefore if the buying power of the currency unit is to be stable wages and salaries must always be paid on a scale that will maintain the right general price level[1] firm under free competition. Also it was pointed out in previous chapters that only under this condition can capital derive its greatest reward in the long run in the changed world conditions.

The part of industry's yield that should be allocated to wages under a steady buying power of the currency unit, the requirement of a rational economy, *is therefore defined*, and this renders easy the allocation to profits and interest. With the part defined which should be allocated to wages, supply and demand can be trusted to determine the part which should be allocated to profits and interest and the relative allocations to these two. If, however, the volume of money available for use is not right, changes in prices may occur independently of changes in wages, and the allocations to wages, profits, and interest may not be in accord with sound economic principles.

It is therefore important that the effects of the

tool for international exchange its effects were highly artificial, and out of accord with sound economic principles. In this chapter no reference is made to international trade and its effect upon prices, as the domestic general price level should be entirely free from any influence of price levels abroad and the exchange rates of the domestic currency in terms of foreign currencies. The exchange system is worked out in Chapters VIII and IX, which would allow the flow of international trade always in harmony with sound economic principles.

[1] The right general price level is defined in Chapter III as the price level which brings about the comfortable employment of all the available labour.

changes in the volume of money available, upon prices and the sound allocations to wages, profits, and interest, be reduced to nil, and that for controlling prices, wages alone be left to occupy the field.

With these objects in view the uses for which money and bank credit should be made available, and the extent, may now be examined.

Loans Eligible through the Expansion of Bank Credit

When goods are finished and ready for the market some time must elapse before they can be delivered from the producer to the consumer. During that interval they must be transported, put in warehouses, and on display, etc. During that interval, assuming that prices are stable, as they should be on the average, goods are not earning anything for any one. On the contrary, expenses are being incurred for transporting, storing, displaying, etc.

Goods are the next thing to money and ordinarily are the safest form of capital against which loans can be made. Therefore goods, after they have been produced, or at least finished to an extent that they can be commonly utilized in commerce, should be eligible collateral against which bank credit can be loaned. Also all bills for goods which have been accepted and which a responsible banker is willing to endorse should be eligible for re-discounting by the central bank.

Each bank-note issued by the central bank against short-term notes and bills of exchange which are secured by goods, really represents a part of the

obligation which was discounted by the central bank, and represents a claim secured by a part of the goods which secured the obligation. Such bank-notes are not only secured by the goods pledged as security, but they are secured by the resources of the purchaser of the goods who accepted the bill, and the resources of the bank endorsing the bill discounted by the central bank. In addition to this the resources of the central bank are involved as security for the notes it issues. If the original debtor and the bank endorsing his obligation could not liquidate the obligation, then the central bank itself would have to deduct the loss from its profits.

If the central bank were a government-owned institution, the taxing power of the government would be a further guarantee that any loss on any obligation discounted by the central bank would be made good. *Better money than central bank money is impossible.*

The carrying of goods with a low charge for interest between the time they are produced and reach the final consumer, by central bank credit, or the community's credit, if the reader prefers, is a service which benefits every consumer.

Next to the loans to the producers and distributors of goods, which are secured by goods, the loans to meet their needs for working capital for payrolls and for supplies not already being carried by bank credit during the period the goods of commerce are in process of manufacture, are the soundest. As a low charge for interest on the working capital required for the production of the goods of commerce also benefits every consumer, and as the risk on such

loans is nil with proper care by the banker, money or bank credit for such purposes should also always be available to the producer or distributor of goods, providing he can convince a prudent banker that there is a demand for his wares and that he can liquidate the loan in a short time.

Obviously, the outstanding volume of money or bank credit required for the above purposes depends upon the rapidity with which the money yield of industry is returned to industry. That is, it depends upon the time which the spenders and savers take for exchanging the money yield they have received, for the goods and services produced by industry, and thus for returning to the producers and distributors the funds with which to liquidate their loans.

Naturally the farmer's loan for buying seed and paying wages must run until his crops are sold, and therefore it must run for a longer period than the glove maker's loan for paying for his leather and his wages. Many services require almost no working capital. A restaurant proprietor practically sells his services before he pays his bills for groceries and wages. The season of the year has much to do with the volume of bank credit required to carry such goods as foodstuffs, cotton, wool, etc.

Bank credit is not a commodity, and *should not be subject to supply and demand.* Bank credit is made merely by book-keeping entries of debits and credits of claims for commodities so that *commodities may be freely exchanged in commerce in harmony with supply and demand.*

The aim of banking policy should be to provide

book-keeping entries of just enough claims for goods and services to permit the comfortable employment of all the available labour, the natural economic condition which would be constantly ruling under the correct economy as pointed out in Chapter XI.

The right to extend bank credit should be deemed a right conferred by the public. The furnishing of bank credit and currency is a public service, and like all other public services it should be furnished to the public at as near cost as practicable.[1]

The cost of rediscounting by the central bank is very small, and the risk is nil under a rational control of bank credit, therefore *the rediscount interest rate should always be low* regardless of the demands for savings for long-term loans. Also it is a service which can be rendered practically as efficiently and safely by the government as by private enterprise.

The loaning of bank credit to individuals, however, is a different matter. The banker must know the borrower and know about the demand for his wares, his efficiency as a manager, etc. The banker must be guided by purely *business* considerations; if he makes mistakes he incurs losses. It is, therefore, a service that can well be left to private enterprise.

The cost of the service which the banker renders, or at least the price he is able to charge for the service he renders, is dependent upon the cost of

[1] There is much talk to the effect that bank credit or the public's credit should be cheap if the best interests of the community are to be served. The credit which the central bank furnishes is the only credit which should be cheap when labour is fully employed. It is the only place normally in which the community's credit should be risked, and in no other place can low-cost credit be used with greater benefit to the masses or without danger of disturbing the rule of sound economic principles in the allocation of wages, interest, and profits.

rediscounting his bills at the central bank. If that cost is low the banker can keep the price he charges for the service he renders lower than he could otherwise. While banking is a public service, it is a public service from which the profits can well be left for determination by free competition, if rational rules for governing banking in harmony with the public interest are laid down.

The amount of bank credit outstanding should be just sufficient to permit the comfortable employment of the available labour, and capital accruing from savings. Labour should always be in brisk demand, and the same is true of savings. This is the condition which ensures economic liberty, and is a condition to be most jealously guarded—*it is the condition which should dominate monetary policy.*

When the point is reached where labour is comfortably employed no further *increases* in the volume of bank credit outstanding for financing the expansion of productive facilities, building, public improvements, etc., should be allowed. From that time onward only savings should be available for such purposes—only the yield from industry should be available for claiming the products of industry. Otherwise more will be demanded than the available labour can produce and prices will rise, thus increasing the profits to bankers and borrowers and reducing the share of industry's yield which can be allocated to labour and savings.

In orthodox monetary practice it is at this point that the rediscount interest rate at the central bank might normally be raised for increasing interest rates

and contracting bank credit, but it is a fallacious tool for what should be the end desired. It increases the cost of financing payrolls for the production of consumers' goods, and increases the cost of carrying goods between the time they are produced and the time they reach consumers, thus increasing the costs of goods to the public. The increased cost of goods to the public is offset by the profits accruing to the central bank and the profits accruing to liquid banks for making book-keeping entries of credits to borrowers which a high rediscount interest rate enables them to collect. If that were all a high rediscount rate did there would not be so much to complain about, but when it starts a wave of deflation with privation and bankruptcy, *which a low rediscount rate cannot check*, it is time to discard such a seemingly innocent, but grossly harmful, tool.

A high rediscount interest rate at the central bank—at the public's bank—has signally failed as a tool for accomplishing anything but serious injury to the public.

A high rediscount interest rate of itself is not so harmful, but when it is used the word is passed around among bankers that deflation is on the way. This causes them to try to become as liquid as possible and naturally they give attention to their long-term loans. They reduce them as far as they can—"when it rains they ask for the return of the umbrella they loaned in fair weather." As fast as their long-term loans are liquidated, they refuse to make others, and they feel obliged to watch their position and to continue that policy after the rediscount

rate is lowered. The result is that the money going into the durable goods' industries is checked and a vicious circle of lower employment and lower consuming power is put into operation. A situation is soon created wherein there seems to be over-production on every hand in the enterprises in which long-term loans are commonly used, and no prudent business man wants a long-term loan then regardless of how plentiful the funds available for such purposes may be. This pursuance of a deflationary policy periodically, which was forced upon the banks by the practice of the gold standard monetary system, was the great error in orthodox banking, and was responsible for the dire consequences of periodical dislocations of industry.

As stated previously, the benefit of a low interest rate for short-term loans for carrying goods and financing payrolls benefits every consumer. As a service furnished by a public institution should always be available to the public at near cost, *the rediscount interest rate should always be low.*

When the point is reached where the available labour is comfortably employed the monetary authority should not raise the rediscount interest rate, it should merely request—with the power, of course, to enforce its request—that the banks *refrain from increasing the volume of their outstanding bank credit* for long-term loans, and that from that time onward any increase in the volume of outstanding long-term loans would have to come from savings.

Then if the volume of bank credit outstanding for carrying goods were above normal, it would signify

that savings were accumulating and that consuming power was falling behind productive power, and *if that condition were allowed to continue* prices would fall. The situation should *not* be dealt with *by any change in monetary policy.* It should be dealt with only by the wages authority, and corrected by raising wages and salaries a little as pointed out in Chapter III. Then with more consuming power taking more consumers' goods off the market and thus indirectly creating a demand for savings for the production of more producers' goods, a further expansion of bank credit for carrying goods would be unnecessary; instead the need would be reduced.

As a matter of fact, when the demand for savings is high, the stock of unconsumed goods is low and the volume of idle savings is low, and a smaller volume of bank credit will suffice to carry the stocks of goods and the funds which are idle between the time they accrue and the time they find employment. Bank credit is more active, but that does not harm bank credit; it makes it more healthy, and *it is a most desirable condition that should be constantly ruling.*

As previously suggested, when labour and savings are in demand, as they always should be, there would be a demand for bank credit for producing durable goods, and if the banks kept themselves liquid, as they would when expanding bank credit only for short-term loans for the carrying of goods and the financing of payrolls in the production of goods, they would, of course, be in an excellent position to expand bank credit for accommodating a high demand for long-term loans. But if they did the bank

credit loaned would be occupying a field that should be open to savings only. A higher interest rate for savings is the best way of encouraging more saving in harmony with sound economic principles, and in harmony with economic liberty.

Loans Not Eligible through the Expansion of Bank Credit

In order to give practical effect to the monetary authority's request that no further expansion of bank credit be permitted except for the short-term loans when labour is comfortably employed, and in order to clarify the situation,[1] the banks should be requested to create savings departments[2] and to turn over to their *savings departments* all outstanding long-term loans. As these loans were liquidated the proceeds would have to be made available to their savings departments for making other long-term loans if sufficient money were to be available for financing projects which required long-term loans, and if the labour and facilities commonly employed in such projects were to continue in employment.

The claims for the yield of industry taken to

[1] The end in view should be achieved by the direct means. To require a higher ratio of reserves to deposits or to raise the rediscount interest rate at the central bank causes real savings to be in competition with book-keeping entries of credits, and permits the banks to collect the same rate of interest on their book-keeping entries as savers receive on real savings. Also short-term money is placed in competition with long-term money, and the interest rate on short-term loans is made subject to supply and demand. Such tools are altogether too crude and indirect-acting for the end in view, and when used for stopping inflation are likely to start a wave of deflation which a reversal of policy cannot stop.

[2] If a bank was not interested in creating a savings department it could transfer its long-term loans to some other bank or institution which was interested in making long-term loans. A bank transferring its long-term loans to another bank or institution would, for reasons which will appear in a subsequent footnote, probably prefer to write down both its assets and liabilities by the amount transferred, and the transferee would similarly write up his assets and liabilities.

liquidate the long-term loans would have to be made available for buying the products of industry, otherwise under-consumption of durable goods would result. For any further long-term loans the banks should be privileged to loan from their savings departments only the savings deposited with them for that purpose.

The banks which created savings departments would encourage the deposit in their savings departments of inactive funds in their banking departments by paying an interest rate in harmony with the supply and demand for such funds.

While the savings department of a bank would keep its idle funds on deposit in the banking department where all its other deposits were kept, theoretically it should not be allowed to borrow from the banking department—the department which, generally speaking, creates more money every time it makes a new loan or investment—or from the banking department of any other bank.[1] It should, of course, be able to borrow from the savings departments of other banks and similarly to loan to other banks.

The interest rate charged for the loans of savings should be governed solely by the supply and demand for savings if sound economic principles are to rule, regardless of how high the demand for savings might be. The time when the demand for savings for expanding industry is highest is *exactly the wrong time* to allow an expansion of bank credit to take

[1] In practice the savings department of a bank might be allowed to get a short-term loan from its banking department to meet an unexpected withdrawal of savings by savings depositors, but such loans should be liquidated before any further loans were made from the savings department.

the place of savings, just the same as the time when labour is in the highest demand is exactly the wrong time to allow rises in wages if equilibrium is to be preserved, as has been pointed out in previous chapters. More money then could serve only to increase productive power by raising prices and reducing the allocations available from industry's yield for labour and savings. This would necessitate higher wages and salaries and lower profits later if the higher productive power were to be employed. The expansion of productive facilities should not proceed much ahead of consuming power on the whole if the best interests of capital as well as labour are to be served. A feast or a famine economy is harmful to the best interests of productive capital. With practically a constant balance between consuming power and productive power, productive power would increase uniformly on the whole.

With the foregoing proposals in effect it is obvious that there would be two basic interest rates for funds, one for short-term loans and another for long-term loans.

The interest rate for short-term loans would always be low and not affected in any way by supply and demand—the cost of making book-keeping entries for expanding and contracting the short-term money available to the public in the public's best interests would always be relatively low.

Also it is obvious that the interest rate for long-term borrowings would normally be materially higher and in harmony with the supply and demand for savings.

Naturally with low-cost bank credit always available for short-term loans for carrying goods and financing payrolls, many concerns which have been in the habit of providing their own working capital for such purposes would reduce their working capital by using it for expanding or improving their productive facilities and/or for distributions to their shareholders. In the best interests of all, the producers and distributors of the goods of commerce should be encouraged to take advantage of low-interest loans for their working capital.

It is obvious that the proceeds from the liquidation of their long-term loans, which the banks turned over to their savings departments when prosperity was reached, would naturally occupy the field with savings, but beyond this only savings would be available for long-term loans.[1]

To summarize. In general the following may be laid down as the essentials of a sound banking policy—

1. When labour is not comfortably employed wages should be raised to restore prices and bring about full employment, and long-term loans should be available to credit-worthy borrowers through the expansion of bank-credit if necessary. The status of employment should be the basis for expanding bank

[1] The long-term loans transferred to the savings departments of banks when prosperity was achieved would give existing banks having a large amount of such loans the benefits of loaning in competition with savings a store of credit which was created by the public's borrowing. Apparently in fairness to the public and in fairness to new banks, and to existing banks not having material assets in long-term loans, a bank having such a store of funds should pay the public—the Government—interest on them in harmony with the interest paid on funds deposited in their savings departments by savers.

credit for long-term loans, not the liquidity of the banks.[1]

2. When prosperity has been achieved bank credit should not be further expanded for long-term loans, thereafter only savings should be available for a further increase in the volume of long-term loans, and the interest rate for long-term loans should be subject only to the supply and demand for savings.

3. Bank credit should always be available to credit-worthy borrowers for short-term loans at a comparatively low interest rate, and not subject to supply and demand in any way.

4. If the volume of outstanding short-term loans and unemployed savings is above normal it should be contracted only by raising wages.

5. The rediscount interest rate at the central bank should always be low.

Investing in Bonds by Banks.

It has been the custom for banks in Great Britain in recent years to buy government bonds and to refrain from making any long-term loans. The central bank's policy of buying government obligations with book-keeping entries resulted in central bank credit being used by the government for paying its bills, and thus more central bank credit soon found its way into the banks in the deposits of those who

[1] The fact that a bank has ample reserves and liquid assets which would enable it to expand safely its bank credit is no excuse for permitting it to do so. Under a sound banking policy in a rational economy which would ensure a steady general price level and a balance between consuming power and productive power, the banking departments of all banks would always be in a very liquid position. Their savings departments would, and should always be, in a very unliquid position.

received government payments. As these deposits of central bank credit constitute reserves in the banks having them, the banks' reserves were increased by the amount of central bank credit deposited with them. By having a higher ratio of reserves to deposits, the banks were thus enabled or permitted to invest in government bonds. The effect, however, of the banks' purchases of bonds upon the volume of claims being presented for goods and services at any particular time may be much the same as if the banks had made long-term loans directly. By the banks purchasing bonds which are held by investors, funds are placed in their hands which may then be employed in long-term loans or for investing in new stock issues, new buildings, etc., directly or indirectly. If the funds find such employment the result is prompt demands for more goods and services. The purchase of bonds[1] by the banking departments of banks is inflationary, and would certainly cause prices to rise if labour and productive facilities were comfortably employed under free competition regardless of whether wages were raised or not.

Also if the banks bought bonds faster while prosperity was being achieved than the sellers of bonds could make use of their funds, there would be a

[1] The glut of unemployed funds in the banks in 1933, 1934, and 1935 resulted from the expansion of bank credit for the purchase of Government bonds by the banks. Bank credit occupied the field with savings that should normally be left to savings alone, with the result that the interest rate on real savings was low. The banks may have purchased lower interest bonds from the Government for retiring higher interest bonds held by individuals, but the effect upon the money seeking investment held by the public was exactly the same as if the banks had purchased their holdings in bonds directly from the public.

store of idle funds when prosperity was achieved, and inflation would continue further.

However, for inflation to continue there must be more and more expansion of bank credit. No matter how far bank credit may be expanded beyond the needs of commerce at any particular time by the purchase of bonds by the banks, inflation would not continue a great way if such purchases were discontinued, and if wages were not raised, and before a great while savings would commence to dominate the field which should be theirs.

The bonds held by banks would, or should, remain frozen in their assets until liquidated, the same as any other long-term obligations or loans.[1]

Off the gold standard a large amount of bank credit outstanding as the result of banks having liberally purchased bonds would in no way impair the ability of banks to accommodate commerce with the sound amount of bank credit to keep labour fully employed, and this is true regardless of how far in the future the bonds might be liquidated.

The effect upon the volume of money and bank credit in the hands of the public at any particular

[1] The banks should, of course, be free to exchange their notes, investments in bonds, etc., with each other. Such transactions have no effect upon the funds in the hands of individuals or in the hands of the Government for investing and/or spending. Likewise the buying and selling of debts or investments between individuals, or between individuals and the Government, have no effect upon the total funds which may be used for claiming the goods and services produced by industry. It must be remembered, however, that the banking department of a bank cannot *buy or sell* a debt or investment from or to the public without increasing or decreasing respectively the volume of funds in the hands of the public available for demanding the products of industry. In general, what a bank may do, and what any other institution or individual may do, may have very different effects upon the volume of claims for goods and services in the hands of the public.

time as the result of purchases of bonds by the banks with book-keeping entries would be exactly the same *if instead* the government had bought the bonds from the holders with printing press money. This may be a shock to many, but it is true nevertheless. For equal purchases of bonds by the government with printing press money or by the banks with book-keeping entries, the amount of funds placed in the hands of sellers of bonds would be exactly the same and the inflationary tendencies would be exactly the same.

The effect, however, upon the public's pocket-books and the banks' profits would be different. The public would be spared paying taxes to cover the interest payments the banks were receiving if the government had bought the bonds instead of the banks. Furthermore, when the time for redemption of the bonds came, the government could either collect from the public the funds with which to retire and destroy the bonds it had purchased, or it could leave the printing press money it had paid out for the purchase of bonds frozen in the bank credit structure permanently.[1] The only difference in the results would be that under the latter plan, (*a*) the public would be spared from taking out of their incomes the taxes with which to retire the bonds the government had purchased, and (*b*) the banks would have greater reserves against which they could soundly expand bank credit for commerce, and thus

[1] It is pointed out in the latter part of Chapter IX that the banks could hold printing press money in their vaults, or in the vaults of the central bank, nearly equal to their deposits without any inflationary effect under a sound banking policy. Preferably the printing-press money outstanding should be well below the minimum seasonal need for money. In France the bank-notes outstanding amount to more than bank deposits.

they would lose less interest to the central bank for the rediscounting of short-term bills of exchange, more of which would otherwise be necessary.

It may seem odd in the minds of many that while vast unemployment is ruling and many industries are greatly depressed, the banks are making large profits which they are paying out in dividends and hiding away in new banking houses and new buildings for other purposes, etc., but there is a reason. The banks will continue to make presents to themselves in this way, and perhaps they should, until public leaders will familiarize themselves with the great benefits to be derived from the rational use of bank credit. The leaders should recognize the restraint which must be practised in the use of bank credit if the best interests of all are to be served. It should be recognized also that there are very definite and clearly obvious considerations which should determine how far bank credit should be expanded in the best interests of all.[1]

If public leaders would take the time to study and grasp the situation they would soon find sound reasons for calling upon the government to request the banks to disgorge their holdings in government bonds and to accept in their place printing press money to the amount the banks paid for their bonds.[2]

[1] Under the gold standard economy the balance in trade was a factor which prevented the accommodation of the public with a volume of bank credit in harmony with its best interests, but under a rational exchange policy which is dealt with in Chapters VIII and IX that hindrance would be removed. Under the gold standard the volume of bank credit outstanding had to be in harmony with the supply of gold in the country.

[2] Economically there can be no complaint against what the banks have done if they have returned all of the taxpayers' money they have received back to industry. There may be a complaint, however, against what the banks have done from the standpoint of social justice.

To do this would not cause the slightest change in the volume of claims in the hands of the public for industry's yield under a sound banking policy. If it were argued that by the banks holding the bonds they could contract the outstanding money available for long-term loans if it should seem desirable, the answer is that the banks' holdings were purchased at near par and are paying a low interest rate, and the banks could not afford to dump them on the market at the prices they would bring if funds were finding employment to the extent that very substantial rises in prices appeared imminent. Incidentally, as will be evident subsequently, to permit a certain volume of bank credit to be outstanding for a time in long-term loans, directly or indirectly, and then contract it later, is one of the worst economic crimes that can be perpetrated against society.

While investing in bonds by banks is profitable and safe enough from the standpoint of the banks, it is a practice which has been brought about through the exigencies in the practice of the unsound gold standard banking policy. If prosperity were ruling, it would be unsound for the government to buy its own obligations from the public with printing press money, as that practice would result in inflation and unearned profits accruing to borrowers at the expense of the buying power of incomes received by the holders of fixed interest securities, and all those having fixed money incomes. *It would always be sound* under a sound banking policy, however, for the government to purchase with printing press money

bonds from the banks which the banks had previously purchased with book-keeping money.[1]

In the present case the banks have already exchanged book-keeping entries for the bonds they hold, and they have placed a vast store of funds in the hands of the public which cannot soundly be taken away from the public, regardless of how great the potentiality of such funds may be for inflation. The potential injury to the *rentiers* which may not be apparent yet has already been accomplished by the banks. There will, however, be compensating advantages to the producers in industry; prosperity would be impossible without higher prices, and higher prices would be impossible without expanding bank credit. To cry out against a certain amount of price-raising above present levels is to cry out against ever allowing the unemployed to go to work again. The bankers have done their part by taking the orthodox method for raising prices, but, as pointed out in previous chapters, prices cannot rise a great deal in the present situation without material rises in wages, under free competition.

It must be recognized that basically the general wage and salary level determines the buying power of the currency unit. It must be recognized that the extent to which prices may rise depends upon the attitude and the collective power of labour.[2]

[1] This remark refers to the banking departments of banks only. Purchases of any kind of bonds could, of course, be made by the savings departments of banks without making any change in the volume of claims in the hands of the public for the products of industry.

[2] As will be evident from what is said in previous chapters, British labour would confer a very great benefit upon Great Britain if it would do its part by bringing about higher prices through higher wages. It is to be hoped, of course, that labour would use its power by getting the

It is time that this factor were clearly recognized and that it were harnessed so that the best interests of both labour and capital will be served. Otherwise there is no telling to what extent prices may rise and to what extent the *rentier* class may be injured. It is time that the allocations to labour, invested capital, and savings be made in accord with sound economic principles which require that the barriers to free competition be removed.

The book-keeping entries already made for the purchase of the bonds by the banks are intended to be scratched off by the banks when the government raises funds for liquidating the bonds. But under the circumstances to collect from the public, including the *rentiers*, the taxes necessary for enabling the banks to scratch off their book-keeping entries will accomplish nothing profitable to any one, not even to the banks,[1]

Government to assume the responsibility of allocating the rises in wages in harmony with the considerations laid down in Chapters II and III for the guidance of a Wages Board. Any worth while prosperity is impossible without much higher wages and, strange as it may seem, higher sterling wages would greatly increase British export trade under a rational exchange policy, which is dealt with in the next chapter.

[1] The rediscounting business of the central bank would, of course, be reduced by a substitution of printing press money for the bonds held by the banks, but its business in rediscounting is already at low ebb because of the glut of reserves already in the banks which was created by the book-keeping entries of the central bank in *its* purchases of Government obligations. What the central bank lost in its rediscounting business would be gained by the banks, and no harm would result to the banks or to commerce under a sound banking policy if the central bank never did much rediscounting. Furthermore, there is no reason why the central bank—the public's bank—should be flooded with transactions that the banks could just as readily and soundly take care of themselves if given the proper facilities for doing so under sound regulations.

The banks would thus gain something if instead of the public taking out of industry's yield the funds with which to liquidate their bonds, the Government gave the banks printing-press money for their bonds. They would, of course, lose profits derived through making the supply of short-term accommodation limited, as they should. The old system under the gold standard of making the charges for short-term accommodation subject to supply and demand would be abolished, as it should be.

and would not only be a very expensive way of scratching off those entries, but it would cause very serious harm to industry.

It is obvious that if no bonds had been purchased by the banks, the taxpayers' money when collected and used in the liquidation of the bonds would be given to the holders of the bonds, and it would thus be available for employment again in commerce and industry. It would be available for claiming goods and services equal in value to the claims given up by the taxpayers, and no inflationary or deflationary tendency would result in the long run.

If the liquidation were accomplished a little at a time possibly it might not be very disturbing to the market for savings and the normal course of industry, but to take taxpayers' money for the purpose of liquidating the bonds held by the banks and for scratching off their book-keeping entries made at the time the bonds were purchased, the results would be entirely different. The taxpayers' money would also be scratched off the banks' books, and not any of it would be available for employment again in industry. A part of the claims for goods and services yielded by industry in one month would disappear and would not be available for claiming goods and services the next.

When a bank makes a loan or buys a bond by creating the funds out of the blue the funds are returned into the blue when the loan or bond is liquidated. When the banking department of a bank makes a new loan it does not loan its depositors' funds; it creates a new deposit, and that deposit disappears when the loan is liquidated.

To liquidate the banks' holdings of bonds with taxpayers' money would reduce the outstanding volume of bank credit and would be deflationary. Just as the purchase of bonds by the banks was *inflationary*, the liquidation of the bonds held by banks would be *deflationary*.

Because a "reflationary" policy had been pursued in a previous period in order to achieve prosperity, that would be no excuse for pursuing a *deflationary* policy at a later period and bringing depression.

Surely it would be a sad reflection upon the intelligence of any people if they burdened themselves by heavy taxes and brought depression upon themselves to *accomplish nothing more useful* than allowing the banks to cancel out book-keeping entries they had previously made.

It is obvious, of course, that when the monetary authority requested, as proposed previously, that the banks turn over their long-term loans to their savings departments, he could have requested at the same time that the banks also turn over their investments in bonds to their savings departments. In that event when the taxpayers' money was turned over for the liquidation of the bonds, the money would again be available in the savings departments of the banks for long-term loans. Also with the banks holding their bonds as they do now, it is obvious that as their bonds were liquidated the banks might be allowed to take on new long-term loans in their place. In either case deflation could be avoided only if the banks were successful in inducing industry to become as much indebted to them as the government had

been, which would be a very questionable policy even if it were possible. They could, of course, buy other securities as an alternative to loaning to industry for avoiding deflation.

But to collect taxes from the public for nothing more useful than enabling banks to loan to individuals and/or to buy securities would not be very constructive to say the least.

The funds resulting from the banks' purchase of Government bonds are non-interest bearing to the recipients, and these funds have gone into the hands of individuals who are employing them in industry. It is one thing for an individual to give employment to his own funds, but quite a different thing for him to give employment to funds a bank might be willing to loan him.

For the banks to liquidate their holdings in bonds by collecting taxes from, or by selling their bonds to, the public, would reduce the money which individuals would want to employ in industry, even though the banks would willingly grant long-term loans to the extent of the funds taken from the public in the liquidation of their bonds.

British banks have enjoyed a privilege in that to a very large extent funds could accrue to a depositor only as someone else paid interest on funds to the banks. The banks issue book-keeping money for loans, or for their investments in bonds, and thus in either case they collect income on the funds which become available as deposits. The only exceptions to this condition are the book-keeping money and paper money issued against the purchases of gold.

The deposits arising from the banks' purchases of gold are small compared with the other deposits upon which the banks have been drawing income indirectly as interest on loans or interest on bonds. The Government has paid debts by fiduciary issues of notes up to £260,000,000, yet the public continues to pay interest on those debts to the Bank of England either as interest on "government debt" or as interest on bonds lodged with the Bank.

If the Government exchanged printing press money for the bonds the banks are now holding it would be merely granting another fiduciary issue in the liquidation of Government debt.

As the amount of such a fiduciary issue is already outstanding in book-keeping money there would be no inflationary effect. It would, however, reduce to some extent the interest that the banks would be able to collect indirectly on outstanding bank deposits in the future if the new fiduciary issue paid no interest directly or indirectly.[1] What the banks lost would be the public's gain.

By the banks being able to control the volume of bank deposits outstanding through their control over their volume of loans and investments outstanding, they had a powerful weapon for effecting deflation and lower prices in their management of the gold standard, while labour could be forced to take lower

[1] There is no more excuse for the central bank's receiving interest upon a Government's fiduciary issue than for the bank's receiving interest upon a note issue against gold lodged with it.

In some countries the militarists have succeeded in convincing their governments that their interests are the centre around which all other interests should revolve and to which all other interests should be subordinated. In other countries the people have been freer from the grip of their militarists, but they have had their gold standard bankers.

wages or starve. Since they have lost their control over wages and prices, fortunately through the dole and the bargaining power of labour, there is no excuse for their having any control over the volume of outstanding bank deposits inimical to the public's best interests.

There is no reason now why the banks should not always pursue a policy in harmony with the best interests of commerce and industry. The potential good the banks have volunteered by placing funds in the hands of investors in exchange for Government bonds has been done and should never be undone.

The greater volume of bank credit outstanding as a result of the banks' purchases of Government obligations and bonds should be frozen permanently into the monetary structure. This could be accomplished in two ways—

(*a*) The Government could avoid ever liquidating the bonds the banks are holding, or

(*b*) The Government could exchange printing-press —fiduciary—money for the bonds the banks are holding.

From the standpoint of the public either course, under a sound banking policy, would be a sound alternative to the deflationary policy of collecting taxes to liquidate the bonds held by the banks. Alternative (*b*) would have the added advantage that the Government debt would be reduced by the amount of fiduciary money the Government turned over to the banks in exchange for Government bonds.

Alternative (*b*) would be much less expensive to the public and, therefore, to continue paying an

interest rate on the bonds, which swells the profits of the banks, could be looked upon by the public only as a subsidy to the banks.[1]

The unearned profits could be taken out of alternative (*a*) by the Government's substituting 99-year no-interest bonds for the bonds held by the banks—tokens could be substituted for the bonds the banks bought with book-keeping money. Such tokens, however, might not be satisfactory to the banks in the exchanges of collateral among themselves, unless they could deposit them at the central bank and draw upon them there. It would seem, therefore, that the simplest and best way to prevent undoing the good the banks have already done would be to give the banks Treasury notes equal in amount to their bonds, which they could deposit at the central bank and convert into central bank notes if they desired.

It may be said that the banks now hold a vast store of Government bonds because of two fundamental errors in previous Government monetary policy—

(*x*) For raising the funds it was spending in the War, the Government had a choice between *taxing* profits and *borrowing* profits—selling Government bonds. It chose the latter course to a considerable, extent, but it is questionable if *borrowing* for non-productive spending is ever sound.

[1] A more fallacious idea never existed than that subsidies and stifled competition are the road to recovery. Instead they are the road to stabilized depression, as pointed out in previous chapters. Subsidies can be looked upon only with suspicion by the public, and if the conscientious objectors to bureaucratic control of industry and regimentation will not give attention to the way prosperity is to be achieved and maintained with wages, profits, and interest being always alloated in accord with sound economic principles, there is danger that economic liberty will be rendered a meaningless term.

(*y*) The Government was led into going back to the gold standard after the War, which was accomplished by deflation with serious unemployment.

Now, in effect, the banks have exchanged book-keeping money for bonds sold by the Government during the War for replacing funds unsoundly taken out of the money system after the War. The banks have utilized error (*x*) for correcting error (*y*). This is undoubtedly the soundest solution, and it only remains to arrange that the correction be made lasting by measures (*a*) or (*b*) previously pointed out, and by the adoption of a sound banking policy also previously pointed out.

To achieve prosperity there must be a certain amount of "reflation," and to maintain prosperity the "reflation" must be made permanent. The banks have issued book-keeping money which is applicable to "reflation." Surely there can be no more constructive method of making the issue permanent and preventing the banks from contracting it than by an exchange of Treasury notes for the Government bonds the banks are holding. This procedure would not only reduce the Government debt by the amount of the Treasury notes or fiduciary money paid over by the Government, but by the same amount it would reduce the volume of debt which must be incurred by individuals to the banks for keeping the wheels of commerce turning.[1]

Under a sound economy all investing in long-term Government borrowings would be left to

[1] On page 223 it was pointed out that banks should be enabled to make long-term loans until labour is comfortably employed. Perhaps a better

the public so that savings would be diverted from their normal uses to Government uses, and thus the equilibrium between the demands upon industry and industry's capacity to deliver would be maintained, otherwise inflation with rises in prices would result.

The business of the banking departments of banks would be to take care of the book-keeping involved by the money transactions of their depositors and *to loan* bank credit to credit-worthy borrowers in the best interests of the public.[1]

method of supplying the long-term money necessary to the full employment of the available labour, if there were not enough long-term money outstanding already, would be some further purchases of government bonds with fiduciary money. In this way long-term money would be soundly available to industry without borrowing from the banks. A certain amount of additional funds would thus be available for employment in industry by those who prefer to pay as they go, and at the same time the public debt would be further reduced.

Certainly the gold standard bankers could not complain if the private holders of government bonds exchanged their bonds for foreign gold and then exchanged the foreign gold for bank-notes which could be employed in British commerce and industry. If the private holders exchanged their bonds for fiduciary money instead of gold the effect upon industry would be exactly the same.

Under a sound banking policy not the slightest harm could result from a goodly volume of fiduciary money; on the contrary it would be a poor money system, and one not suited to a people who prefer to pay as they go, as they should, if a bank deposit could accrue to one individual only as some other individual incurred debt and paid interest to a bank. There is no reason why 90 per cent of all outstanding bank deposits should be always paying interest to the banks directly or indirectly.

Formerly gold coins upon which no bank was drawing interest were freely used in commerce, and there is no reason why, under a sound banking policy, there should not be a good supply of fiduciary money available for use in the same way.

Because book-keeping money pays interest to the banks that does not necessarily make it sounder from the public's best interests than fiduciary money.

[1] Under a rational economy and a sound banking policy it might develop that the banks would not earn as high dividends as they have been in the habit of earning, and that they would find they have more capital tied up in their business than the earnings and the lower risk involved under a sound banking policy justified. In that event their shareholders would find ample profitable employment for their unneeded capital in other branches of commerce and industry under stabilized prosperity.

Other Activities of the Banks.

Under a sound economy, depression and deflation throughout a country would become a pestilence of the past, and bankers could safely loan against more obligations of commerce and industry than they have been in the habit of doing. As the savings of the public accrue in the banking departments of the banks it would seem that the banks should be in an excellent position to borrow the public's savings and make use of them in their savings departments for long-term loans.

Banks often act as investment brokers which, in view of their position with the public, is a natural and constructive service for the banks to render.

Sometimes banks go so far as to act as investment trusts. In the U.S. this has been particularly true of private banks. There is a question, however, if they, or any other organizations, should be allowed to form investment trusts with the view of diverting the control of corporations away from their founders and normally elected successors for the purposes of making consolidations and eliminating competition. If consolidations or increases in capital are desirable then the effecting of them can generally be left, with advantages to the public, to the normally elected officers of the individual corporations concerned.

Speculation in the development of a new productive enterprise which does not make profits, or save losses, by making someone else poorer, and which tends to increase the supply or lower the cost of a commodity, is constructive speculation beyond question.

Speculation in the earning power of producers, or in the prices of commodities produced and consumed by others, without rendering service, is not very constructive, because its gains in the end must come from the pockets of producers and/or consumers.

It has been argued that the interest rates charged could be used as a weapon against the operations of speculators in their efforts to corner markets in the products of the earth, and in their efforts to inflate stock market values, etc. High interest rates are practically no deterrent to such efforts, and are harmful to those engaged in legitimate business. Also, in connection with the Producers' Marketing Boards suggested in Chapter IV, the margin which they could borrow against the stocks of their products should be limited, especially when their stocks are above normal. In all such cases it would be best to deal with the offenders against sound business direct. In the past there have been altogether too many attempts to deal with abuses in business by indirect methods which have been harmful to the innocent bystanders, instead of dealing with them directly out in the open.

While loaning funds for financing non-productive speculators may be safe enough from the banker's standpoint, more goods could be consumed if the non-producers became producers. Therefore it would seem that the banks should, at least as far as practicable, not be allowed to be a party to assisting in the diversion of the fruits of industry from the pockets of the producers to the pockets of the non-producers.

Government Borrowing.

It has been stated that the Government loans its credit at a low rate of interest and pays a high rate of interest for its borrowings, and the question has been asked whether the Government need do so.

Let us consider the Government's ability to finance large expenditures. The Government's credit is good because of its ability to levy taxes and collect revenue, and it is, of course, limited by the sums it can collect in this way, just as an individual's credit is limited by the money he can collect from the sale of goods. The Government usually meets the current demands upon it from current collections of revenue, or by short-term borrowings which it can repay with the revenue that will be due and collectable in a short time.

No inflationary tendency can result from the loans of claims against industry's yield by book-keeping entries, which will be shortly liquidated by yield collected from current production. Therefore the expansion of bank credit to accommodate the Government's short-term requirements for funds is quite as devoid of inflationary tendencies as the other short-term loans discussed in previous sections.

To expand bank-credit when labour is fully employed for loans of claims for industry's current yield, which will be liquidated some years later, would be issuing claims for more yield than can be currently produced, and prices would rise, which is to be avoided. Therefore when labour is fully employed

the accommodation of the Government's long-term borrowing should be only from savings.

Government financing in time of War is dealt with in Chapter XI.

Was the War Financing Equitable?

The War was paid for out of the savings accruing during the War. At the close of the War the Government owed much of the cost of the War to those who stayed at home and loaned to the Government from their high incomes made during the War. By this method of financing the War, the difference in the financial position of those who stayed at home and those who went to the front was very marked. Undoubtedly, if another war should come there would be some discussion as to whether the method used in the last War was the correct method of financing war expenditures. Taxes could have been levied upon the incomes of those who stayed at home, or industry conscripted, as were the fighting men, so that the War would have been paid for as it progressed.

Under any sound plan of financing the War it would have been necessary that all the money used by the Government should be saved out of the proceeds of industry during the War. As it was necessary for the Government to spend large sums, it was necessary for the Government to encourage saving, and to restrict spending by the people. The people should now do the spending, and the Government should encourage spending and the enjoyment of higher standards of living in every

sound way. The rate of production is limited absolutely by the rate of the spending.

The great advantage to Great Britain of being free from the gold fallacy during the War should serve as a lesson in how to prosper in peace time by being free from the gold fallacy. Any nation which thinks it must borrow from abroad in order to finance its own efforts to expand its commerce and industry, is labouring under a delusion which will hamper its progress. It has failed to profit by the monetary experience of the War, and to realize how readily its own central bank credit and banknote currency may be expanded to accommodate the full and efficient productive power of its own people.

The Quantity Theory of Money.

The believers in the quantity theory of money have argued that if the Government would increase the money outstanding in times of depression by large purchases of gilt-edged securities with central bank money, commodity prices would be raised. The fact is that such purchases place the new money mainly in the hands of investors and not in the hands of spenders, and have little, or very slow, effect upon commodity prices. Large amounts of idle money in the hands of investors, it is argued, would inspire them to undertake projects which would give employment to labour and thus indirectly increase consuming power. With the consuming power well below the existing productive power, however, there is not much incentive or opportunity for investors to employ their idle funds profitably in new productive

projects. The result is that what money is invested is invested in new buildings,[1] etc., on the expectation of a low profit yield compared with previous experience, and the impression is that the yield for savings will always be low. This causes the market value of all income-producing equities to be high relative to their profits when considered in the light of previous experience.

The U.S. Government has also been attempting to restore prosperity by encouraging the banks to buy Government bonds, and the Federal Reserve Banks have been buying Government bonds freely. The result is that individuals have a store of idle funds and the banks have large holdings in bonds which are yielding good profits to the banks, and also the banks have large deposits in the Federal Reserve Banks. Instead of being heavy borrowers at the central bank, as was the former practice, they are now large depositors with the central bank.

This policy is having a marked effect upon stock market prices, and there is apprehension that inflation is on the way and that the value of money is to be reduced. If this policy continues and stock market prices are inflated beyond reason, a hectic scramble

[1] The banks' purchases of government securities in Great Britain have resulted in a vast store of funds being employed in building, but with so much unemployment ruling the labour organizations have made little headway in raising wages, the fundamental requirement for raising prices and achieving prosperity in the present situation. The labour organizations have also been handicapped in raising prices through higher wages because of the orthodox belief that high wages would reduce British exports instead of greatly increasing them.

To attempt to achieve prosperity through the banks' purchases of government securities, and without raising wages, the purchases will have to continue or there will be a falling off in the demand for labour in the building trades, and at best it can prove only an emergency effort. More is said about a rational exchange policy in Chapters VIII and IX.

to convert money into durable goods will set in, and a boom in building and in other industries will be precipitated. But even then the amount prices rise will depend very largely upon how much wages are raised.

The large amount of bank credit outstanding as a result of bank and Federal Reserve Bank purchases of bonds during 1934 and 1935 affords a base for a tremendous bank credit inflation under U.S. banking practices. Under the orthodox banking policy of the U.S. when prices rise sufficiently to bring about full employment, the monetary authorities would doubtless try to restrict further inflation by demanding an increase in the ratio of reserves to deposits and/or by raising the rediscount interest rate. But by using these orthodox but grossly crude tools only, the monetary authorities would be likely to start a vicious wave of deflation which could not be checked by reversing their policy. The effect of mass psychology in such an unsound situation makes it difficult to predict what may happen, but, regardless of what happens, the Government of the United States will continue in a very embarrassing situation until the transcendent economic importance of wages is recognized and intelligently utilized.[1]

[1] What the central bank or the Treasury would do with its gold when a sound banking and exchange policy was adopted will be found in Chapter IX.

CHAPTER VIII

CORRECT EXCHANGE POLICY FOR A NATION ACTING INDEPENDENTLY

THE desire in each nation for an unvarying exchange rate of its currency with that of other nations is a delusion that has been responsible for much of our undoing. The exports of each nation are only a small part of the total of all its production, and the international money transactions involved in the goods exported are few in number compared with the many internal money transactions involved in the production of even only the goods exported. Yet, for the sake of stability in the exchange rate for the few external transactions, we sacrifice stability in the purchasing power of our currency unit for the great many internal transactions, and bring trade cycles with serious economic maladjustments upon ourselves.

It is time we brought intelligence to bear on the cause of so many of our economic ills, and realized that prosperity can be made continuous under industrialization only by the use of a currency unit the purchasing power of which is *constant in home markets* and *adjustable in foreign markets* for the purpose of keeping our exports in the correct balance with our imports.

While an international clearing association, which is discussed in the next chapter, would be *much simpler* in operation *and better in every way*, and is bound to function as the future international

exchange mechanism, let us first note how a single nation acting alone could soundly master its international exchange problem.

The Gold Standard Method of Conducting International Exchange.

Before discussing a better way of conducting international exchange it may be well to review how in principle the exporter is paid by the importer under the gold standard system of international banking. A bank in London which makes a speciality of trade settlements between London and New York has a branch in New York, or a correspondent in New York, which is interested in giving the same kind of service for New York as the London bank gives for London.

For the purpose of our discussion we will assume that the name of the London bank is the Thames Bank, and that it conducts its exchange transactions through the Hudson Bank of New York, and that these two are the only banks directly involved in our exchange transactions so far as our exporter and importer are concerned.

A British importer, desiring to get 1000 bales of cotton from a certain American exporter, would go to the Thames Bank and explain his desire and arrange satisfactory terms with it for paying it in sterling for the cotton after the cotton is received in England. The Thames Bank would then notify the Hudson Bank to pay the American exporter the sterling equivalent in dollars for the cotton when he presented proper papers to show that the cotton had

been shipped, insured, etc. The importer in London would pay the Thames Bank in accordance with the terms arranged with it in the beginning after he received the shipment of cotton.

In a similar way the Hudson Bank of New York would accommodate an American importer who wished to get a shipment of woollen goods from Great Britain. In that case the American importer would arrange to pay the Hudson Bank in dollars for the goods imported, and the Thames Bank in London would pay the equivalent in sterling to the British exporter for the goods exported. In other words, the business of the Thames Bank in London would be to receive sterling payments from British importers and to pay out sterling to British exporters. In the same way the business of the Hudson Bank in New York would be to pay out dollars to American exporters and to receive dollars from American importers. For these accommodations to exporters and importers the Banks would be paid a small percentage charge on the payments involved.

If the respective exporting and importing transactions balanced each other over a period, no gold would be moved between the Thames Bank and the Hudson Bank during that period. If the exporting and importing transactions did not balance each other, gold might be moved to the Thames Bank from the Hudson Bank or *vice versa* to make up the balance. On the other hand, if the Thames Bank owed the balance to the Hudson Bank, for instance, it might find that the Jones Bank belonging to its London Clearing House Association had a balance due

it from New York. In that event the Thames Bank would pay the Jones Bank the sterling equivalent of the dollars it owed the Hudson Bank, and the Jones Bank would instruct the bank owing it in New York to pay the dollars to the Hudson Bank.

In a similar way, if the Hudson Bank in New York owed the Thames Bank in London, it might find similar accommodation in New York for paying the Thames Bank in London. In this way the international banking houses of London and New York co-operate with each other and derive mutual profits from not having to ship gold either way, unless there is a decided unbalance in the total of the payments due in London and New York.

The "British Clearing House" Plan.

The exchange plan now to be proposed really amounts to nothing more than a British Clearing House through which all British exchange transactions would be cleared. The "British Clearing House" would pay British exporters in sterling for the goods exported, and the British importers would pay it in sterling for the goods imported. On the other hand, the "British Clearing House" would pay the foreign exporters in foreign currencies or in foreign credits for the goods imported into Great Britain, and the foreign importers would pay it in foreign currencies or foreign credits for the goods exported from Great Britain. The British Treasury would merely act as arbiter or act as the owner of the Clearing House, and would set the respective sterling exchange rates so as to keep the payments

made abroad in approximate balance with the payments received from abroad with a view to keeping the respective exchange rates as steady as practicable over long periods, and with a view to encouraging a free and steady flow of international trade, without the trade cycle and the hardships and injustices inevitable in the gold standard method.

While sterling has been "off" the gold standard for over four years at the time this is written, gold is being used in British exchange transactions much as before, the main difference being that gold has no fixed value in terms of sterling. It still has fixed values in terms of other currencies, and for that reason it has value in exchange and is regarded as foreign currency in the plan which follows. When it ceases to have a fixed value in terms of any currency its *artificial* value in exchange will be lost, and harm to the nations from putting their trust in it will end.

As will be shown later in this chapter, gold could cease to have value at any time without materially handicapping the effectiveness of the plan proposed. How gold could cease to have any value without material loss to the Treasury of any nation will be explained in Chapter IX.

It is suggested that the proper measures for Great Britain to effect in the present circumstances would be as follow—

1. Great Britain's Treasury should take over the mastery of its own house and control sterling exchange rates through conducting all sterling exchange transactions in Great Britain itself—in effect, making any private sterling exchange transactions

in Great Britain a criminal offence. The Treasury, in effect, would scrutinize all sterling exchange transactions, *just as a Government scrutinizes many other international activities, which are of much less importance to the well-being of the nation.*

2. The Treasury would designate certain banks as its agents for conducting international exchange transactions, always at the rate of exchange set by the Treasury. The agents would be required to report daily to the Treasury the amounts involved, and the nature of the exchange transactions taking place.

3. The Government would confine its activities, in connection with banking and foreign exchange, solely to (*a*) rediscounting through the central bank certain short-term commercial and Government obligations tendered to it by sound banks, *always at a low interest rate and without limit;* (*b*) decreeing changes in the wage and salary level for achieving the proper purchasing power of the pound in Great Britain, making such changes as small and as few as practicable; and (*c*) exchanging sterling for foreign currencies and *vice versa*, and changing the exchange rate of its currency so as to preserve the proper balance between its exports and imports, making these changes as few and as small as practicable.

4. The Treasury, by paying out sterling, would take over at the existing exchange rates all monetary gold and foreign currencies in Great Britain not already in its possession through the holdings of the Issue Department of the Bank of England. The sterling paid out by the Treasury for this purpose would be central bank-notes or Treasury notes,

the same as would be given in exchange for gold under the gold standard.

5. The exchange agents would pay out sterling against the Treasury's account, in exchange for foreign currencies or gold coming to Great Britain as payment for goods or services exported, or coming to residents of Great Britain from their foreign investments; and, conversely, the exchange agents would exchange foreign currencies or gold belonging to the Treasury for sterling, for the purpose of paying for foreign goods or services imported into Great Britain, or of making payments due to foreigners on their investments in Great Britain.

6. The exchange agents would exchange sterling into foreign currencies, or *vice versa*, in the necessary amounts for the convenience of travellers, etc., without hindrance, but would prohibit any transactions which savoured of speculation in currency or international investment through exchange.

Great Britain is suffering from the effects of too much freedom in international investment. The returns on foreign investments made in previous generations are depriving the industry of the present generation from the benefits of producing the equivalent of all the goods consumed in Great Britain. It is, therefore, clear that in her own best interests Great Britain should in the future discourage the investment abroad of capital created in Great Britain. As, off the gold standard, the inflow of capital into Great Britain through international exchange adds to the disadvantages experienced from the inflow of the incomes from foreign investment, Great

Britain, in her own best interests, should likewise discourage the inflow of capital into Great Britain through international exchange. The Treasury, therefore, would require an investor desiring to invest in another nation to purchase British-owned securities of that nation, which he could exchange in that nation for what he desired. This would reduce the incomes on foreign investments which are paid by goods imported for which no goods are exported. Likewise, the Treasury would require those desiring to invest in Great Britain to purchase foreign-owned British securities, of which there are also plenty, which the investors could exchange in Great Britain for what they desired. This would permit capital to be imported by a corresponding export and without receiving it in the form of goods for which no goods could be exported. More is said about international investments in Chapter X.

7. By decreasing sterling's purchasing power for British products, that is, raising commodity prices by increasing all wages and salaries, internal credits now frozen would quickly become liquid, and with a low rediscount rate foreign floating credits would become almost useless as such in Great Britain for financing the internal commercial operations of Great Britain. Therefore, if the owners of short-term credits wished to take them away from Great Britain, they could do so by the method suggested above, or by exchanging them for British-owned foreign credits. If the owners of short-term credits retained them for a time in British industrial or commercial securities, it is likely that they would

not fare badly. In case, however, the owners were unable to invest or transfer their short-term credits in terms of sterling before a little sterling "reflation" took place, they would suffer only the loss of a profit that has inequitably accrued to them during the past few years, which all owners of currency or credit must lose if any prosperity is to rule in their respective nations in the near future. The suffering from such losses would be very mild compared with the despair which has been visited upon a vastly greater mass of humanity by deflation.

8. Any foreign tourists who enjoyed the many free public roads, beautiful parks, educational and recreational facilities of Great Britain, and who brought with them all their own means of transportation, food, clothing, sleeping and living accommodation, and all the goods and supplies of every nature which they consumed while in Great Britain, would not be very welcome visitors. Yet those people who live in Great Britain on foreign-produced incomes, which cause Great Britain to receive an excess of imports of goods and services over exports, are doing this very thing. Great Britain's best interests would not be harmed in the least if many such individuals emigrated to enjoy their incomes in the lands which produce them.

Therefore, Great Britain's best interests would not be harmed in the least if equitable taxes were imposed upon all incomes from abroad when sterling is off the gold standard. On the gold standard a nation often hesitates to protect itself from practices harmful to its industry by measures which would in

any way cause a reduction in the amount of gold coming to it.

9. The Treasury would set the exchange rate so as always to keep a proper balance in foreign currencies or foreign credits, and gold on hand. Normally, this balance would be just sufficient to provide adequately for the demand for foreign currencies required for paying for imports of goods and services into Great Britain, or for the export of earnings on foreign-owned investments in Great Britain. There would be no object in bringing about a greater excess of exports over imports than was necessary for meeting the Government's foreign obligations, as the burden of financing any important excess under sound management would fall upon the Government. Also, there would be no object in allowing imports to exceed exports, which would waste Great Britain's purchasing power on goods giving no employment to her own resources in labour and production facilities. It would be impossible to carry this practice far, however, without exhausting the Treasury's supply of foreign currencies, which, in turn, would cause sterling's exchange rate to drop abroad, disclosing bad management on the part of the Treasury. Therefore, the Treasury would strive to keep sterling's exchange rate at the right point to bring about the desired balance between exports and imports, and it would strive to make the changes in the exchange rate as small and as few as practicable.

10. In case the British Government wished to make a payment to another Government, the Treasury would lower sterling's exchange rate so as to bring

about the desirable excess of British exports over imports. This would bring an excess of foreign currencies or credits to the Treasury's international exchange account, which the Treasury could use in making the desired payment to the foreign Government. The sterling currency used by the Treasury in paying British exporters for the excess of exports over imports would be raised by internal taxation, as would ordinarily happen under the gold standard when the British Government made a payment to another Government.

If the British Government wished to receive a payment from another Government, it *could* accept foreign currency. The Treasury in effect would first convert such foreign currency into foreign goods and then convert the foreign goods into sterling. It would do this by raising sterling's exchange rate so as to bring about the desired excess of imports into Great Britain over exports, using the foreign currency received from the foreign Government for paying for the excess of imports.

The excess sterling currency coming to the British Treasury from the excess of imports over exports would be used to reduce the tax burden upon the people living in Great Britain.

In comparing these two inter-governmental debt payments it may be observed that in the first illustration Great Britain as the debtor paid the creditor in foreign currency, having *first* sold abroad the goods necessary to the payment. In the second illustration Great Britain as the creditor received the debtor nation's currency in payment. In this case the goods

necessary to the payment would be sold abroad in effect by the debtor *after* the payment was made.

In connection with the second illustration it may be observed that if an "unbalance" in international investing and speculating were prohibited, then any of a nation's currency paid out by its Government to a foreign creditor or paid out by its inhabitants for foreign goods could find its way back to that nation again only in payments for goods or services produced by that nation, and the nation would thus be unable to get into a debtor position which would be harmful to its industry and commerce.

11. In conducting international trade, it is often necessary to enter into engagements which cannot be liquidated until some months later. As the parties to such engagements are concerned only with the amount of their own respective currencies involved, there is no reason why the Treasury should not assist its international commerce by protecting the parties to such *bona fide* transactions by guaranteeing the exchange rate for some months ahead on all such engagements registered with the Treasury's duly authorized bankers at home and its duly authorized agents abroad, all such transactions being reported promptly to the Treasury in the same way as the current exchange transactions would be reported. The Treasury could alter the exchange rate of its currency at any time, and the volume of guaranteed future exchange transactions outstanding would not affect in the slightest the financial position of the Treasury, or the parties to the registered transactions for future liquidation. By keeping a register of future

exchange commitments as well as of current transactions, the Treasury could regulate the exchange rate more intelligently than when depending upon current and past transactions only.

Other suggestions are made in the next chapter in connection with the operation of an international clearing association, which would be applicable to the international exchange plan here being considered. Also the advantages of regulating the exchange rate to maintain the proper trade balance are pointed out later in this chapter and in Chapter IV.

In conducting her foreign exchange by the method outlined, Great Britain would be enabled to maintain sterling at the desired equitable purchasing level in Great Britain, and would be enabled to provide currency and credit for her own commerce and industry at a low cost, doing full justice to herself, and *without the least injustice to any other nation*, sterling would soon be commanding universal esteem.

With Great Britain only off the gold standard and all the other nations on, Great Britain would merely set the exchange rate of sterling with gold and this would automatically set the exchange rate of sterling with all the other currencies. However, with more or all the nations off the gold standard, and with proper care, an exchange rate for each nation's currency would soon come about which would keep each nation's exports balanced by its imports and which would tend to be fairly stable. As previously pointed out, no nation would benefit from carrying an excess of foreign currencies in its Treasury, beyond the amount necessary for its

imports and foreign obligations. If Great Britain had an excess of foreign currencies, she would raise the exchange rates of sterling, and if she were short of foreign currencies she would lower the exchange rates of sterling. There could be a considerable disparity between the rates set by Great Britain and the rates set by foreign agencies for their respective currencies, but this would cause no harm in Great Britain with private international investing and speculation through British exchange under control.

In an exchange transaction between two nations having a disparity in the exchange rates set for their respective currencies, the exchange would be naturally effected in or by the agency offering the greater amount of the exporter's currency per unit of the importer's currency. This would always cause the flow of the foreign currency or credit to the agency bidding the most for it, and thus assist it in satisfying its demand. Also future commitments would be guaranteed by the agency offering the more favourable rate to the payer.

In the conduct of foreign trade, one nation is often a heavy exporter to a nation from which it imports little, the latter exporting mainly to some other nation. This would cause the former to have an excess of a foreign currency or credit which it could not use directly and to be short of a currency or credit for which it had direct need. This would require exchanging the excess currency or credit for the currency or credit it was short of, with another nation. Possibly several exchanges might be necessary before getting the accommodation desired.

In conducting exchange in this manner, Great Britain's exchange organization, and the exchange agencies of foreign countries, would quickly find that it paid to co-operate in getting the accommodations they required, and any disparity between the exchange rates offered in one country and in another country would tend to be small.

All the disadvantages of the plan here proposed would be entirely overcome, and very great advantages to all nations would accrue if, as is suggested in the next chapter, they all joined an international clearing association, which is bound to be the enduring international exchange system of the future.

Higher Sterling Prices would Improve British Export Trade.

With gold out of the picture, the exchange rate of sterling would rest upon its buying power in Great Britain for British goods and services. At the present time the exchange rate of the pound in American money is about five dollars. Disregarding the effect of the present tariffs, a British exporter of a certain grade of hats to America, for instance, could get one pound sterling per hat by selling to an American importer who would pay five dollars per hat.

If, for instance, British wages were raised so as to double British prices the British exporter would have to get two pounds sterling for a hat which he formerly sold for one. With the exchange rate of the pound resting upon its buying power in Great Britain,

however, sterling's exchange rate would be halved if sterling prices were doubled, and in terms of dollars one pound would be worth only two and one half dollars. Therefore the American importer's five dollars would be just as attractive to the British exporter for a hat as before, because with the five dollars he could then get two pounds, the new price of his hats, through international exchange. Therefore, higher British prices would offer no hindrance to the export of goods out of Great Britain.

If wages were raised so as to double the prices of British-made goods and services and so as to halve the exchange rate of the pound, it would mean that all British imports would cost the importer twice as much in sterling as before. The sterling cost, however, of any British-made substitute for an imported article would also be doubled so that the foreign article, in comparison with the British substitute, would be just as attractive to the British consumer as before. Therefore a lower exchange rate of the pound resulting from higher British prices would offer no hindrance to imports into Great Britain.

With wages and salaries raised so as to raise British prices materially and bring prosperity to Great Britain, the demand for raw materials and other foreign goods would increase, and with the exchange rates of the pound relative to other currencies adjusted so that Britain's exports would balance her imports, there would be a corresponding increase in British exports.

By discarding British protective tariffs, importing

would be further stimulated, and exporting would be correspondingly stimulated.

The Way to Remove Tariffs against British Goods.

Assuming that an equivalent of 30 per cent duty on all imports is required to keep British imports in balance with exports and income on foreign investments, then if all British tariff duties were discarded sterling's exchange rate would be lowered 15 per cent to maintain the balance, not 30 per cent. The net effect of this would be to lower the cost of British goods to foreign buyers about 15 per cent, and to lower the cost of foreign goods to British buyers about 15 per cent,[1] which would greatly stimulate importing and exporting, and British shipping would soon be taking on new life and enjoying prosperity along with other British industries.

By Great Britain setting the example of discarding tariffs and managing sterling's exchange rate to keep British exports in the proper balance with imports, with only benefits to herself and other countries, other countries would quickly see the logic of her system and adopt it also. By removing their tariffs and lowering their exchange rates sufficiently to compensate for the removal of their tariffs, the cost of British goods to foreigners and the cost of foreign goods to British buyers would again be reduced, and thus international trade would be further stimulated to the mutual benefit of all countries.

[1] Thirty per cent decrease due to tariff removal, less 15 per cent increase due to the 15 per cent lower sterling exchange rate, leaves 15 per cent.

Assuming that all countries now have the equivalent of, say, 30 per cent tariff duties on all imports, then, with all countries discarding their tariffs, the goods of each country would be about 30 per cent cheaper to foreign consumers and foreign goods would be about 30 per cent cheaper to its consumers under approximately the present exchange rates.

With a clear understanding of the examples cited, it is not difficult to understand why tariffs have been so ruinous to international trade, and how if all tariffs were discarded there would be a healthy need for much more shipbuilding. The standard of living of each country would be raised materially through being able to exchange goods costing it less to produce for foreign goods which would cost it more to produce.

To bring about free trade, *tariffs must be discarded.* To use tariffs as a bargaining lever for unsound preferential trade agreements, as many statesmen have been advocating, is exactly the wrong way to bring about free trade. All should buy in the lowest market and sell in the highest in the best interests of the standard of living in their own country as well as that of the rest of the world.

The advantages of international trade to a country "are far above the petty interests of this industry or that industry," in the words of Mr. Cordell Hull. "The slogan, 'Buy at Home'" is fallacious because it really means, *Don't Sell Abroad,* but without a sound exchange policy much foreign trade leads to foreign loans and proves a snare and a delusion.

No other country could object to Great Britain's reducing sterling's exchange rate 15 per cent if she reduced her tariffs 30 per cent.

Fixed exchange rates bring tariff barriers and are a hindrance and not the help to international trade that many suppose.

It is impossible to exaggerate the advantages to all countries of *natural* exchange rates for their respective currencies under free trade. A worthwhile prosperity in the Machine Age is impossible under the fixed exchange rates of the gold standard which require harmful tariffs and/or the more harmful juggling with the rediscount rate and contraction of bank credit for the purpose of keeping the payments made abroad in balance with the payments received from abroad.

Under the gold standard wages had to be sufficiently low in Great Britain always to permit British goods to be sold abroad and the lower wages were, or the lower the standard of living in Great Britain, the more Great Britain was able to sell abroad.

Under the correct international exchange policy, the higher the standard of living in Great Britain, the more Great Britain would sell abroad.

Under the changed world conditions, the lower British wages are the less Great Britain will be able to sell abroad, and the higher British wages are the more she will be able to sell abroad. Civilization has advanced to a point where Great Britain will never again be able to increase her export trade by lowering wages.

Correct Exchange Policy would Eliminate Competition between One Country's Labour and Another's.

When the other nations stop paying Japan, for instance, in gold for her surpluses of exports over imports, Japan will be forced to take goods in exchange for her goods, and she will be able to export more goods than she imports only by pursuing the former policy of Great Britain of investing her surplus credits abroad. That policy would temporarily benefit the Japanese industrialists, but Japan would soon find that the incomes on her foreign investments would later force her to import more than she exported with the same harm to her industry that Great Britain has suffered.

With Japan forced to take goods in exchange for her goods, the lower she kept her general wage and salary level in terms of the yen, the lower would be the yen prices of her goods and the higher would be the exchange rate of the yen, and Japanese industrialists would be unable to gain any unfair advantage in foreign markets through low Japanese wages.

With gold out of the picture, goods could be exchanged only for goods, and a country having the lowest standard of living for its workers would not have the slightest advantage in foreign markets over a country enjoying the highest standard of living for its workers on the whole.

Japan for some years exchanged her silk for American cotton. Assuming that Japan's foreign trade consisted only in exchanging silk for cotton grown in America and America's foreign trade

consisted only in exchanging cotton for silk produced in Japan, then the amount of silk Japan desired to exchange for cotton would depend upon the relative costs of producing silk and cotton or substitutes for cotton in Japan. Likewise the amount of cotton the U.S. would desire to exchange for silk would depend upon the relative costs of producing cotton and silk or the substitutes for silk in the U.S. The wages paid in dollars in the U.S. and the wages paid in yen in Japan would have no bearing upon those respective relative costs, and cotton and silk would exchange on a basis that would equalize America's desire for silk with Japan's desire for cotton regardless of America's general wage level in terms of dollars compared with Japan's general wage level in terms of yen.

Furthermore, American labour would not be in competition with Japanese labour, on the whole, to the slightest degree. It is true that America's labour engaged in producing silk would be in competition with Japanese labour having a more favourable environment for producing silk, and employment for American labour for producing silk would be reduced. On the other hand, however, employment for American labour for producing cotton in a more favourable environment would be increased. On balance American labour would be saved by producing cotton instead of silk. The labour thus saved would be available for producing other goods which would raise America's standard of living. Japan would enjoy a similar advantage from her view-point. This free trade in cotton and silk between America

and Japan would improve the standard of living in both countries.

For Japan and the U.S. to agree to trade with no other nations would of course be contrary to the best interests of both, as they would both greatly benefit by being able to exchange freely the products they were well fitted to produce for the products of other nations which they were not so well fitted to produce. Also they would not wish to be restricted to having their exports to each nation balanced by what they imported from it. They would merely want the total of all their exports to be balanced by the total of all their imports, and neither would want its workers to be in competition with the workers of the other nations, on the whole. Their wishes in these respects would be gratified up to their fondest hopes, and in a simple, logical, businesslike way under the exchange plan proposed in the next chapter, which has a thoroughly sound and scientific basis.

In 1927 some of the high priests of the gold standard might have objected that by leaving gold out of the picture, international trade would degenerate into "international barter." To-day the hopes of the gold standard adherents would be realized to the fullest if gold could only prove an effective instrument to that very end. But it is altogether too crude and unscientific for modern needs and is thoroughly unjust to the workers of a modern nation. The workers of a nation must remain in competition with the workers of other nations having lower standards of living as long as it adheres to the gold standard or adheres to *fixed exchange rates* of its currency with

other currencies, unless it resorts to protective tariffs which would deprive it of the great advantages of free trade, or unless it resorts to other complicated and unbusinesslike measures which will be discussed in the next chapter under "Fixed Exchange Rates."[1]

[1] If in the transition to a higher price level and prosperity in Great Britain, a British contractor found himself obligated to furnish a big order to Australia, for instance, which required a long time to execute, the contractor would sustain a loss especially if his payment was specified to be made in sterling. If his payment was specified to be made in Australian currency, and if Australia's price level did not change until after he received his payment, he would probably not sustain a loss, because his Australian pounds would exchange for more sterling pounds than he anticipated at the time his obligation was contracted.

Such cases, however, would be few, and, undoubtedly, the contractor and buyer could work out a settlement which would prevent undue loss to the contractor resulting from a rise of wages in Great Britain and a lower exchange rate of sterling. Even though they could not, it would be no excuse for continuing low prices which cause depression and unemployment.

CHAPTER IX

INTERNATIONAL CLEARING ASSOCIATION THE IDEAL FOR INTERNATIONAL EXCHANGE AND LIQUIDATION OF INTERNATIONAL DEBTS

ALLOWING the exchange rates of the various bank-note currencies to be determined by international bankers acting through their own agencies and independently and without using any gold, would prove far less disturbing to the continuous well-being of the nations involved than settling trade balances by the gold standard practice. It must be remembered that a currency unit which has a buying power for goods in its own country has real value, and that international bankers can utilize that value in making international trade settlements. Gold has had special value in international exchange only as the currencies to which it was artificially tied have had value.

The method of conducting international exchange by the Treasury of a nation assuming responsibility over the exchange rates of its currency for other currencies, and forcing all exchange transactions within its confines to clear through one organization and thus enable the rule of more stable exchange rates, as proposed for Great Britain in the previous chapter, would be a vast improvement. However, an ideally perfect system in any possible international situation would be afforded through the operation of an international clearing house association.

An international clearing association would be of special advantage in liquidating the present War debts, and, for reasons which will be more apparent later, the best interests of all nations would be served by organizing an international clearing association at the earliest date possible.

For the moment let us disregard the effects of the present international debt situation, which is dealt with later in this chapter, and let us assume that those nations having currencies of stable purchasing power for the average of a wide variety of commodities consumed in the respective nations—and having confidence that each would always act for its own best interests—form an international clearing association, having branches in each member nation, each member nation being REPRESENTED on an international clearing association committee BY AN OFFICIAL OF ITS TREASURY STAFF.

International Clearing Association would Hold No Currency.

The operation of an International Clearing Association would be similar to the operation of a "British Clearing House" described in the first part of the previous chapter, except that it would be simpler. The Treasury of each nation would have only the responsibility of paying its own exporters with its own currency received from its own importers, and of providing its own credit to pay its exporters when its total exports exceeded its total imports, as would happen occasionally to some degree in its own best interests.

In order to get the idea of how an exporter would receive payment through an international clearing association for the goods he exported, let us first reduce an international trade transaction to the simplest terms. The actual steps and the machinery involved will be described later in this chapter, and compared with present practice they will be found simpler and less expensive to both importer and exporter.

Suppose, as an example similar to the one used in the previous chapter, that an importer of cotton in Liverpool agreed to purchase 1,000 bales from an exporter in New Orleans for £8,000, and suppose one pound sterling was worth $5 in international exchange, the importer would make payment for the cotton by delivering £8,000 sterling to a branch of the international clearing association in Liverpool. The clearing association would (*a*) make a note of the transaction, (*b*) give the importer a clearing association order on the *U.S. Treasury* for $40,000, which the importer would forward to the exporter in New Orleans, and (*c*) deliver the sterling received by it from the importer *to the British Treasury*.

In the same way an importer in New York would get similar accommodation through the New York branch of the "I.C.A." for paying the U.S. Treasury for a shipment of woollen goods from an exporter in Manchester, and for having the exporter in Manchester paid in sterling by the British Treasury.

By this system the importer would get the foreign goods and the Treasury of the importer's nation would get the money the importer paid for the foreign

goods. In effect, a nation's Treasury would pay its exporters for the goods exported, and its importers would pay the nation's Treasury for the goods imported. The exporting and importing transactions would offset each other.

In this way no currency would pass into or out of the nations involved. With equilibrium in international trade, practically the same effect is brought about now through the agency of international bankers and their clearing associations—the exporters being paid from the payments made by importers.

The respective clearing association branches would of course accommodate those requiring funds for travelling in foreign countries, and those wishing to transfer funds for other purposes in harmony with the policies of the countries concerned. Such transfers would be regarded as payments for imports and so handled in the clearing association accounts.

In the clearing association operation a nation would not be concerned as to which nations took its exports and from which nations it received its imports. Its only concern regarding exports and imports would be that in the total the payments it made in exchange transactions were in approximate balance with the payments it received.

Whenever a nation's international sales exceeded its international purchases, its Treasury would be obliged to furnish, by internal financing, the currency demanded of it by the international clearing association for paying its exporters for its excess of exports over imports. As will presently appear, the burden involved by this *internal financing* to cover

excess of exports over imports would be nothing compared with the serious weakening effect upon the debtor nation of balancing its excess of imports over exports by *external financing*, as is required under the gold standard.

If the exporters of a nation continued to sell more into foreign markets than its importers bought from foreign markets, then raising the exchange rate of the creditor nation's currency would reduce the purchasing power of the other nations' currencies for the creditor nation's goods, and would increase the purchasing power of the creditor nation's currency for other nations' goods. This would decrease the creditor nation's exports and increase its imports, relatively, thus enabling the unbalance to be corrected.

A change in the exchange rate of a nation's currency would act upon both sides of its foreign trade account—exports as well as imports. Also any adjustment of the exchange rate to restore the desired balance between exports and imports would bear upon *all* exports and *all* imports. Therefore a small percentage change in the exchange rate of a nation's currency would be quite as effective in restoring the desired balance as a much larger percentage change in its tariffs, which usually apply to a comparatively few classes of imports only, under the gold standard. Thus by a change in the exchange rate, the proper trade balance would be brought about with a minimum of disturbance to any of a nation's industries.

As a matter of fact, errors would be made in the

first fixing of the exchange rates for the respective nations' currencies in international trade. Such errors would cause goods to move too freely from some nations, and not freely enough from others, tending to create important credit and debit balances in the international clearing association accounts. The clearing association committee, in co-operation with the Treasuries of the nations concerned, would correct this by adjusting the exchange rates of the respective nations' currencies so as to keep the international trade balances always reduced to as small amounts as practicable, consistent with hindering international trade as little as possible. The variations in exchange rates, however, would become less with a little experience, and would tend to become very small in time, as the natural parity of one nation's products with another's would not change very quickly with the stable prosperity resulting from the use of currency units of constant purchasing power in the respective principal nations.

If a nation were using a currency not regulated to a constant purchasing power within its own confines, the clearing association would take pains to keep such nation's international trade transactions as closely balanced as practicable.

The "International" the Standard of Exchange Value.

In practice, the various currencies would be rated in "internationals"—that is, so many pounds sterling would be required to purchase the hypothetical unit of international value set up by the international

clearing association, which could be called an "international," and likewise dollars, francs, marks, lire, etc., would be rated in the same way. Such ratings with the "international" would facilitate quick calculation of the exchange rate of one nation's currency with another's. The clearing association would take pains to keep the value of the "international" stable.[1]

The liquidation of future international commitments could be made in terms of "internationals," or in terms of the currency of one of the nations involved, just as the interested parties preferred, though in practice such commitments would generally be made in terms of the payee's currency.

No Friction in Clearing Association—Interests Always Mutual.

The operation of the clearing association system would keep the nations involved constantly informed as to the amount of the debit or credit in their international trade, just as under the system described under "2" on page 252, and all the exports and imports designated as "invisible" under the present system, and which affect international exchange, would be constantly and fully visible.

The interests of the nations involved would be so entirely mutual that there could never be much occasion for friction in the clearing association regarding the exchange discounts or premiums required to keep their respective clearing association accounts balanced. A creditor nation would not care to be left carrying the financial burden for a

[1] The means for keeping it stable will be discussed later in this chapter.

great amount of over-selling by its exporters. A debtor nation would not be very happy holding in the clearing association account of its Treasury currency which represented the amount of the over-buying of its people and the amount spent for goods giving no employment to its labour and production facilities, and from which it derived no tax benefit.

If the clearing operations were effected by any other means, quite important surpluses of a nation's currency and credit would tend to accumulate outside the nation's confines, and this could serve no purpose useful to such nation.

The small expense incidental to the operation of such an association would be met by a small equitable fee for each exchange transaction. No nation would permit any currency exchange transactions within its confines except by its duly authorized agents.

The branch offices of the I.C.A. in each nation would be under the jurisdiction of the nation's Treasury.

No Interest Involved in Financing "Unbalance" in International Trade.

As suggested previously, the international clearing association committee would strive to keep the international trade transactions of each nation as closely balanced as practicable. It would be impossible, however, to keep them exactly balanced, and it would not improve matters much to be constantly changing the exchange rates back and forth for that purpose, as this would tend to hamper international trade. The nations would find it better to put up with a moderate "unbalance" one way or the other,

from time to time, rather than experience the disadvantage of frequent changes in the exchange rates.

The Treasury of a creditor nation would be required to pay out to its exporters more of its own currency than its importers paid in. Under "super"-sound management a creditor nation's Treasury *could* finance its needs for its own currency, required to meet its excess of exports over imports, by short-term loans from its own nationals. A nation which paid interest on the funds for financing any excess of exports over imports when it was in the creditor position could soundly use the funds which accumulated in its Treasury from an excess of imports over exports when it was in the debtor position, for paying ordinary current government expenses, and to that extent it could save interest on borrowings for general purposes. If the periods when a nation was in the creditor position could be offset by periods when it was in the debtor position, so that the excess of interest paid when it was in a creditor position would be balanced by the saving of interest when it was in the debtor position, then no interest would be involved in financing the "unbalances" in international trade.

Much better and quite as sound results would be attained if the Treasury of a creditor nation paid for the nation's excess of exports over imports with "printing-press" currency or credit issued by itself, so long as the exchange rate of its currency was managed so that all such currency or credit would occasionally be retired, or nearly retired, by an increase in its imports as compared with its exports.

No practical harm would be done the creditor nation's well-being in this way, as long as its credit balances in international trade were kept within reason. To be consistent, a nation which financed its excess of exports over imports without borrowing should not use for current government expenses the currency accumulating in its international exchange account from an excess of imports over exports when it happened to be in the debtor position. By following this system a nation would never lose any interest in financing its "unbalance" in international trade, and, therefore, there would be no stress to keep its exports always exactly balanced by its imports. There would, therefore, be no need for frequent fluctuations in exchange rates.

International Trade Payments Simplified—No Interest while Goods in Transit.

Compared with present practice, the receiving of payments by the exporters and the making of payments by importers would be materially simplified. An importer desiring to receive a consignment of foreign goods would arrange for his banker to agree to pay his branch of the international clearing association for the goods when they were received. The I.C.A.'s acceptance would be forwarded to the exporter. When this acceptance, together with the insurance policy and the shipping documents, was presented to the exporter's local branch of the international clearing association, the latter would give the exporter an order on the Treasury of his nation for the amount involved at once. Thus the exporter would get payment from his nation's Treasury

promptly after he made shipment, and the Treasury of the importer's nation would be paid promptly by the importer's banker through his branch of the clearing association after the goods were received. The importer would pay his banker for the goods imported at the time and on the terms arranged with his banker when the foreign goods were ordered. In this way, under the plan of financing an excess of exports over imports with "printing-press" currency or by government credit, which would be thoroughly sound, neither the importer nor the exporter nor their respective nations would lose anything in interest while the goods were in transit. If the exporter and the importer were a great distance apart, the acceptance by the importer's branch of the clearing association could be cabled to the exporter, so that any delay in the transaction would be avoided.

As ordinarily in every transaction the importer and exporter are interested only in the amounts of their respective currencies involved, they should be enabled to protect themselves against any loss due to a possible change in the exchange rate of their respective currencies between the time the commitment was entered into and the time the payments were finally completed by the importer. This would be accomplished by making the commitment in terms of the exporter's currency, and arranging so that the importer could protect himself by immediately having his commitment registered by his banker with his branch of the clearing association. In this way none of the interested parties to a transaction would incur any loss or gain through any change in exchange

rates between the time the importer's obligation was registered with his branch of the I.C.A. and the time his payment to his banker was entirely completed. It would, of course, be possible for an importer to lose through competition if other competing importers were able to get the same kind of goods after an important rise in the exchange rate of the importer's currency, and sell them before the earlier purchase had been completely disposed of. In a similar way, an importer could profit by a fall in the exchange rate of his currency. While there would be this risk of price changes through changes in the exchange rate, with a little care in regulating exchange rates such risks would become materially smaller than the ordinary risks of price changes from other causes.

The vast sums of floating private funds now finding employment under the gold standard in financing international trade shipments, and in financing the "unbalance" in international exchange transactions, would be released for use in other channels, highly beneficial to commerce and industry, and probably equally remunerative to the possessors.[1] At the same time the very damaging effects of high rediscount rates and shortages of money upon the well-being of debtor nations would be entirely avoided.

[1] The discounting and acceptance houses of London have done a thriving business in accommodating international trade transactions, particularly before the War. In recent years New York has taken a share of the business.

Under a sound international exchange system, the need for such services would largely disappear. The earnings of the banks and houses specializing in this business were nil compared with the losses sustained by British industry through the periods of deflation necessary to the adherence to the gold standard which made their earnings possible.

A more effective means for paralysing industry than contracting the volume of money below that which has been in use does not exist.

No Nation can Sell more than it Buys.

Compared with the system now in use, traders would find their problems of international trade and exchange considerably simplified. The greater the swing from equilibrium in any nation's international trade, the greater would be the pressure of the corrective forces. Those desiring to export would notice that the ease with which their goods moved into foreign markets would depend upon the ease with which foreign goods came into their own markets.

There would be a tendency for those desiring to increase their export trade to consider how their own nation could use more of the goods of the nations into which they wished to export, and thus the present international rivalry in foreign trade would tend to give way to international co-operation.

It is true that by this system of settling international trade balances, no nation would receive more in the long run for goods and services and payments from foreign investments than it paid out. This is equally true now in the long run, except for the very slight effect of the gold which is produced currently; but now, when equilibrium is much disturbed, the forces involved in the operation of the gold standard result in throwing us further from equilibrium, and if protective duties and/or embargo of gold exports are not resorted to, we have a stampede pushing all the gold into one corner, and then a world trade breakdown.

Liquidation of War Debts.

The unsoundness of the present War debts position and the futility of the efforts to liquidate them under

the gold standard have been becoming more and more obvious for some time.

Let us consider how the international clearing association plan would lend itself to the liquidation of the War debts—debts which really resulted, as will be more apparent in Chapter XI, from the operation of the fallacious monetary system with which, in turn, the attempts to liquidate its own havoc were again threatening civilization.

Each nation could notify the clearing association regarding the instruments of foreign indebtedness of every kind it now holds, so as to clarify the situation as far as possible. Using the U.S. as an example of a creditor nation, the U.S. Government holds foreign notes of indebtedness for which it has already completed the obligation for carrying the capital account—that is, it has floated internal loans, and is now itself paying interest charges upon them. All such instruments would stand as a credit to the U.S. in the clearing association.

International Debts can be Liquidated only by Creditors Taking Unfavourable Trade Balances.

The present War debts, under the gold standard, or under the exchange system here proposed, can be liquidated in the end only through the creditor nations accepting debit balances in international dealings. *If the U.S. had loaned gold, her allies might be able to pay in gold, but as the U.S. loaned goods, her allies can pay only in goods.*

Under the international clearing association, the U.S. or any creditor nation could choose then between taking such unfavourable trade balances or bearing

themselves the interest and liquidation charges arising from their credit balances. If the U.S., for instance, decided to reduce her burden in this respect, then, with the removal of the harmful influence of gold, which has so often caused the good intentions of nations to go wrong, the U.S. could proceed with the business-like liquidation with more assurance, as it would then be able to judge more accurately what was taking place and the readjustments its industry could stand without harm. The Governments of the debtor nations could also proceed in liquidating their indebtedness with much more confidence, once the usurious burden and unstabilizing and disorganizing influence of gold were removed from international exchange.

With the credit and debit balances involved, international trade could not take quite the same natural paths it would if such balances were out of the way. It might be advisable to regulate the paths of international trade by international agreements, but, with care, the natural total volume of such trade need not suffer. The U.S. could start off by agreeing to take, for instance, rubber, tea, and coffee, articles which she does not produce, from the countries producing them, with the understanding that the U.S. would not allow certain of her products to be sent to the countries producing those commodities, and that the U.S. would agree to accept certain specified yearly debits approximately in her international balance in trade. It is believed, however, that the sounder course would be to regulate the yearly balances in trade by adjustments of the exchange rates in the clearing association.

By closely watching her internal commerce and allowing it to develop gradually and naturally into fulfilling new wants or present wants more fully, the U.S. could gradually accept greater international trade balances against her, further reducing her tax burden, and further liquidating the international credits in her favour, with higher living standards and/or more leisure for her people at the expense of the living standards and/or the leisure of the people of the debtor nations. This could all be done without interfering with the bargaining and price-setting between exporter and importer, exactly as now, neither of them realizing that their respective Governments were liquidating debts through these transactions.

If it turned out at the end of any period that the U.S. purchases from abroad had not exceeded her sales abroad sufficiently to suit her fiscal policy, then, in co-operation with the debtor nations involved and the international clearing association, the currency of the U.S. would be placed at a greater premium. This would tend to give U.S. currency more purchasing power for foreign goods, and give foreign nations' currency less purchasing power for U.S. goods, which would decrease the U.S. exports and increase the U.S. imports relatively.

Accounting in Liquidation of War Debts.

By accepting a debit balance in international trade, the U.S. Treasury at the end of the year would receive more U.S. currency in its clearing association account than was paid out, to the amount of such

debit balance. The U.S. would be privileged to use such surplus in U.S. currency for paying interest and liquidating charges on the foreign obligations for which it is responsible to its own people, thus reducing the tax burden on its people and, in effect, distributing to all its people the benefit from the payments on the foreign debts owed to the U.S. In the clearing association accounts, the balances owed to the creditor nations would be reduced by the amounts of their respective excesses of imports over exports, and the debts owed by the debtor nations would be reduced by the amount of their respective excesses of exports over imports.

The Government of a debtor nation would raise the money for paying its exporters for the excess of exports over imports by taxation.

With the clearing association, all that would be necessary for the liquidation of an international debt would be for the creditor nation to buy more than it sold in world markets, and for the debtor nation to sell more than it bought. It would be immaterial with which nations the buying and selling transactions took place, as by the clearing association operation it would be possible for a debt between two nations to be liquidated without any transactions whatsoever taking place directly between the two nations involved.

Each nation would gradually change over from the system of conducting exchange transactions described in the previous chapter to the clearing association operation by gradually transferring its foreign currency and its foreign credits to the clearing

association at existing exchange rates. In their place it would accept credits in the clearing association in terms of its own currency. The clearing association would transfer the currency and credits so delivered to it to the nations from which they originated, debiting such nations in the clearing association accounts for the amounts involved in terms of their respective currencies at the said existing exchange rates. In this way some nations' credits would be more than extinguished by their debits. Any nation could appear as a creditor nation in the clearing association accounts only as some other nation or nations appeared as owing the association.

In the clearing association accounts a debtor nation would not be listed as owing an account to some other particular nation. All nations would be listed merely as creditor nations or debtor nations with the clearing association. No nation would have any outside accounting except with the clearing association, thus reducing the accounting for international settlements to a minimum.

By the method of international settlements proposed, it will be noted the creditor nation would have its foreign trade disturbed, and would continue for a time to have important interest obligations to meet. This is approximately what happens when a merchant mismanages his business by extending too much credit in internal commerce.

As the debts neared liquidation, the U.S. could gradually reduce the yearly balance in trade she would accept against herself, and take the necessary

measures to expand gradually her export trade, so that when her credit balances were extinguished, her exports would equal her requirements for foreign goods. With the debts entirely wiped out, the world could then have absolutely free trade, and would have an equalizer that would keep all nations on an even keel. International co-operation would automatically replace international rivalry and friction.

While economic justice would dictate that no interest be paid to creditor nations upon the credit balances normally accruing in their favour from time to time in the clearing association, such a rule was not in effect at the time the War debt settlements were negotiated, and there is nothing inherent in the machinery of the proposed international clearing association plan that would hinder the payment of interest by the debtor nations upon their War debts. If the creditor nations persist in allowing their intelligence to be obscured by their fetishism for gold, and refuse to accept goods in payment of their debts, they stand a good chance of losing not only interest, but also a large part of the principal as well, to say nothing of the misery which must be endured if they persist in muddling *along* under the gold standard—they cannot muddle *through*. There is also the grave risk that the patience of the sufferers may be tried beyond the safe limit. The nations are all suffering from the results of their own offences against sound economic law, most of them innocently committed. In working out a settlement of our unhappy predicament, it will probably be well not to look for too many motes in each other's eyes, or to worry much

about who has been the greatest transgressor in the past; but rather to be guided by what will be best in the future for all concerned. This generation will be forgiven for making some compromises now if it places future generations on such a basis that a similar situation cannot again arise.

In international obligations, it would probably be fairest if creditor and debtor arrived at a compromise based upon the purchasing power of the respective currencies at the time the obligations were contracted.

In belonging to an international clearing association, a nation's Treasury would manage many of its affairs much as is proposed for Great Britain in Chapter VIII.

To Join Clearing Association and Obligation of Membership.

In joining an international clearing association, a nation which was neither debtor nor creditor would bind itself in no way except to sell as much as it bought in international commerce. A debtor nation would bind itself to pay its international debts by an excess of exports over imports, and a creditor nation would bind itself to accept payments of international debts owed it by an excess of imports over exports. A nation staying out of the clearing association would get along quite successfully, and would be master of the exchange rates of its own currency as long as it managed its exchange rates so as to maintain a surplus of foreign currencies and credits in its Treasury under a plan similar to that proposed in the last chapter.

But it would always have the burden of maintaining, independently, suitable exchange agencies abroad. The exchange rates fixed by the clearing association would be very helpful to the outside nation in fixing its exchange rates with the various other currencies, and the many benefits of an international clearing association would make membership in it prove both an obligation and a privilege to each nation.

While free trade is bound to be the best policy for every country in the long run, and while the attainment of that desirable end by the most business-like means would be the object of an International Clearing Association, no country need be under any obligation to practise free trade always. If for any reason a country thought it advisable to encourage an industry for which it was well-fitted the Government could adopt a tariff policy for protecting it while it was being established.

Industrialists often seek protection, and even subsidies for a new industry, giving as their excuse the country's need for it in case of war. With the operation of an International Clearing Association, which would give each country the great advantage of free trade, the cause of war would be removed. (This is more particularly dealt with in Chapter XI.) Then all countries would find that the advantages gained through free trade would prove a far more effective barrier against war than all their facilities, however great, for the production of the implements of war. They would find, as the U.S. and Canada have found, that unfortified frontiers are a far surer guarantee of peace than all the howitzers and

bombing planes, with which they could be cluttered. In case of war, however, no trader in a nation belonging to the clearing association need have any anxiety about funds or credits in a foreign bank, because under the operation of the I.C.A. no such funds or credits need exist in the conduct of his operations.

The Value of an " International " in International Clearing Association.

On page 276 it is stated that the international clearing association would take pains to keep the value of the "international" stable.

The author would suggest that an "international" be about equal in value to £100 sterling. This would avoid the necessity for using fractions or decimals in rating the various currencies with the "international." At first, the various currencies would be rated with the "international" in about the proportion that their recent respective gold values bore to each other. On this basis to start with, one "international" could equal 100 pounds sterling, 487 dollars, 12,450 francs, 2,045 marks, 9,260 lira, etc.

In the beginning it would be desirable, of course, for the clearing association committee to make as good a guess as possible of the relative values of the various currencies that would cause a balance between the payments made abroad and received from abroad by each nation.

The clearing association committee would be committed to a policy of keeping the value of the "international" as nearly stable as possible.

In general, the committee would raise the exchange

rate of the currency of a country having an excess of exports over imports, and would correspondingly lower the exchange rate of the currency of a country having an excess of imports over exports, and would make no changes in the exchange rates of currencies of the nations whose exports and imports were in approximate balance. Following this practice with care, would tend to keep the value of an "international" stable.

The present international governmental debts, and the measures required to bring about their liquidation would offer a little handicap to keeping the value of the "international" stable that would be avoided if the debts did not exist, but if due care were exercised, and proper allowances made for this condition, the value of the "international" would not need to vary appreciably.

The committee would consider the importance of the currencies not much involved in the liquidation of government debts as an assistance in anchoring the purchasing power of the "international."

Also if any of the nations were not careful about regulating their currency units to a constant purchasing power within their own respective confines, the committee would make due allowance for such lapses, in its endeavour to maintain an "international" of unvarying value.

With proper care, the committee would be able to hold the value of the "international" stable for all time. Any variation at any time would be very small compared with the chronic variation in the *artificial* value of gold in the past.

In an industralized world, seeking the great advantage of free trade between nations, the use of gold as an international standard of value is about as appropriate as would be the use of a ploughed roadway for Rolls-Royce transportation.

Fixed Exchange Rates.

Mr. A. de V. Leigh, of the London Chamber of Commerce, has been advocating an international clearing house plan in which the various nations would agree to "immutably fixed" exchange rates for their respective currencies. However, for one nation to agree to an "immutably fixed" exchange rate for its currency with another nation's currency, regardless of how much the other nation might change the buying power of its currency, would be a condition to which no nation could subscribe with fairness to its own best interests. Nothing in nature remains "immutably fixed."

For a nation to join in the operation of an international clearing association with the object of allowing its currency unit to find its *natural* exchange rate—a rate which would keep its payments abroad in approximate balance with its payments received from abroad—with the other currencies and with the object of keeping that rate as stable as possible under free trade, would be an altogether different matter.

Even under the gold standard, the exchange rates of the various currencies do not remain fixed. When a sufficient disparity takes place, the gold movement point is reached, and gold moves from the debtor country to the creditor country and prevents a

further disparity. Under a correct international exchange system a sufficient disparity in the respective exchange rates should be allowed to take place so that a "goods movement point" would be reached and more goods would move from a debtor country, and less goods would move from creditor countries to it relatively, thus preventing a further disparity in exchange rates. The unbalance in a nation's international trade account should be corrected without resorting to any tariffs or bounties on imports and exports.

Fixed exchange rates for its currency with those of other nations would cause a nation much the same handicap as tying its currency to gold, including the gross injustice of placing its labour in competition with the labour of other nations having a lower standard of living. It could maintain the purchasing power of its currency at a constant level at home with exports in balance with imports only by resorting to tariffs and bounties.

In order for a nation to maintain exports in balance with imports under Mr. Leigh's plan, and at the same time to enjoy the advantages of free trade, if it found its imports exceeding its exports it should levy a tariff on all imports and use the funds so collected for paying bounties upon all exports. In the same way, if it found its exports exceeding its imports it should tax all exports, using the funds so collected for reducing the cost of all imports to importers. To enjoy the benefits of free trade in this way, the effect of collecting taxes on imports or exports and using them as bounties upon exports or

imports, would be exactly the same as the effect of a change in the exchange rate of the nation's currency unit, except that a change in the exchange rate would be far simpler, and more businesslike.

With each nation adjusting its tariffs and bounties on imports and exports independently, to keep their respective exports and imports in the correct balance, there would be confusion, and one country's adjustments would often nullify or accentuate the effect of another country's adjustments, and such confusion would injure the stability of the real exchange rate. To arrive at the "real exchange rate" of any two currencies in such cases, the taxes and bounties on exports and imports of the respective countries would all enter into the calculations.

For the above reasons, and those stated elsewhere, a much better and simpler exchange system would be afforded in every way through the operation of an international clearing association, allowing it to fix the exchange rate of each nation's currency with the "international" so as to keep its exports in approximate balance with its imports with as little variation in the exchange rates as possible.

Disposal of a Government's Gold and Silver.

The U.S. has silver coin and silver certificates issued against silver in its vaults, but the value of the metal is now depreciated below the value of the currency it was intended to secure; many Governments have gold coin and gold certificates issued directly against gold in their vaults, which, under a sound currency system, would also undoubtedly depreciate below the value of

the currency it now secures. The Bank of England and many nations have currency which has been issued against no collateral or commodity security of any kind, and a high rediscount rate has no power to contract any of the currencies mentioned.

With the present depreciation in the value of silver, the currency outstanding against silver amounts to little more than "printing-press" currency. Also the same would be true of the currency now outstanding against gold when gold's value depreciates. But no inflationary tendency would result as long as the banks are restricted to expanding bank credit for no loans other than short term loans after labour became comfortably employed as is proposed in Chapter VII.

Naturally, the "printing press" currency in excess of the amount required for pocket money would be deposited in the banks, and it would act as reserves against which credit entries in the banks' books could be written for short term loans. The "printing press" money in the banks would be quite as useful for reserves against which short term loans could be made as central bank credit derived through having bills rediscounted at the central bank. A large store of "printing press" money would reduce the amount of interest the banks would lose to the central bank. Also, with the banking departments of banks prevented from making any loans, except short term loans when labour is comfortably employed, it will be obvious that no inflationary tendency would result if the banks had a store of "printing press" money practically equal to their deposits.

The banks would probably deposit a large amount of the "printing press" money with the central bank and thus their reserves would be deposited with the central bank. Then when one bank wanted to transfer funds to another bank it would merely write a cheque on the central bank without having to sell bills and lose interest to the central bank in order to get the funds.

With the outstanding volume of bank deposits well above the volume of "printing press" currency outstanding, including that issued against gold and silver in the central bank's, or preferably the Treasury's, vaults, it is obvious that if the value of gold and silver depreciated to nothing, the value of the currency issued against the gold and silver would not suffer in the least. Therefore with a sound bank-note currency system established, the best interests of the U.S., for instance, would be served by gradually disposing of the Treasury's stock of gold and silver at the best prices obtainable, just as it would be desirable to dispose of the stocks of wheat and cotton now held by the U.S. Government at a fair price.

Gold and silver are very useful metals and they should be available solely for use in the arts. A more chaotic national and international economy is difficult to imagine than that which results from hiding gold and silver away in vaults and making them the basis of a most *unnatural* and fallacious monetary and exchange system.

Those Affected by Demonetization of Gold.

To quote from the author's *World Depression to World Prosperity*—

It will be said that with such a drastic move as that proposed, the gold industry would suffer. This is true. With such an unsound feature in our economic structure, many would be inconvenienced in the transition to a sound basis, but any suffering would be infinitesimal compared with the suffering which would be removed from the others of the present generation through a way out of their present intolerable situation and the hope that would be given to those people now in abject poverty through their bondage by gold—to say nothing of the peace and happiness of future generations.

So far as the workers in the gold industry are concerned, they would soon be absorbed into other industries producing the essential commodities, which would quickly take on new life. Normally, much of the gold produced is a by-product in the production of other metals. Johannesburg, however, would be injured seriously, but with gold, which is largely an export trade, out of the picture, all the other South African export trades would flourish.

If we all realized that the purchasing power of gold fluctuates widely, if we could accustom ourselves to keeping wages in gold value in line with the purchasing power of gold, if we could liquidate our debts in gold on the basis of the purchasing power of gold at the time our debts were contracted, if we could accustom ourselves to varying our appraisement of the gold value of all property and all commodities and all services of every kind with the varying purchasing power of gold, and if we could educate ourselves to adjust readily our wages and all price levels to a gold value that would keep our exports in the proper balance with our imports, we should then find the use of the gold standard less disturbing to our commerce and industry, and we should cease to have depression ruling continuously in some debtor nations and prosperity and depression ruling in cycles in creditor nations. However, to

accustom ourselves to all these variations would require the continuous exercise of a degree of intelligence and unselfishness of which most of us are incapable. The constant readjustments required to be made would tax the abilities of the most fair-minded expert accountants.

Long before we could achieve the necessary degree of mental and moral perfection, we would realize the utter uselessness of the gold for the ends desired and the needlessness of the expense in providing it.

The settling of international trade balances in harmony with the best interests of *any nation* by the gold standard method is impossible for any extended period. The gold standard has been the monkey wrench in the machinery of international commerce too long.

The operation of the gold standard is altogether too crude, and dependence upon it by intelligent people for any degree of continuous well-being in the Machine Age will be beyond the power of the future to understand.

CHAPTER X

INTERNATIONAL INVESTMENTS

UNDER the operation of an international clearing association, investments abroad could be made exactly as under the gold standard, and if the wages in any nation were not regulated so as to keep the purchasing power of its currency at an equitable level, profits would tend to accrue for which there would not be employment in that nation. The investing of such profits abroad by individuals of a creditor nation might serve to enhance the foreign buying power for the creditor nation's goods for a time, exactly as under the gold standard. Later, however, the income from foreign investments, through international exchange, would operate to force the creditor nation to take adverse trade balances in goods and services, disturbing its industrial equilibrium and benefiting the industry of the debtor nation, also exactly as under the gold standard.

The ill-effects of foreign investing have not been more generally recognized for several reasons—

(*a*) While foreign investing is under way, exports often materially exceed imports, and industry flourishes.

(*b*) A considerable period must elapse before the tide turns and the incomes from foreign investing cause imports to exceed exports.

(*c*) In seeking the reason for the depression which

follows, many involved symptoms obscure the real cause.

Investing Abroad Differs from Investing at Home.

There are important differences in the conditions which surround investing at home and investing abroad.

Any amount of capital belonging to one part of a nation may be invested in another part without causing the slightest inconvenience in transferring the capital to where it is to be invested, or in transferring the earnings on the investment to the investor.

One part of a nation may always ship to other parts very much more in goods and services than it receives from the other parts. The capital of a nation could be largely owned in one part and production could be largely carried on in another part without any handicap to the nation's continuous industrial equilibrium. Goods are permitted to move freely from one part of a nation to another, and workers enjoy similar freedom. Because of that freedom, prices and wages are kept equalized throughout the nation, and wages and the general price level of the nation can change without affecting the ability of one part to sell to another part.

In the case of investing in another country however, the situation is quite changed. The exports of each nation must be kept in approximate balance with its imports, and goods and workers are often not allowed free movement from one nation to another. The effects of these handicaps

to foreign investing are illustrated by some of Great Britain's experiences.

When British capital was invested in the U.S., there was no trouble in transferring the funds involved through international exchange under the gold standard, because Great Britain was enjoying favourable trade balances; and if all the investments made in the U.S. were not paid to the U.S. indirectly in British goods, there was plenty of gold in Great Britain with which the balances could be paid directly.

After British investing had proceeded for a time, the U.S. had to make large annual payments of earnings on British investments. To make those payments, the U.S. had to have an excess of exports over imports each year equal to such payments, otherwise the U.S. would have had to give up gold. As the amount of gold available for such purposes was limited, the U.S. had to impose tariff barriers and cut down her imports in order that her exports would exceed her imports sufficiently to make the income payments due to Great Britain without losing gold. Thus Great Britain, in order to receive income on her investments in the U.S., was forced to suffer a loss of export trade, and her investments abroad have changed Great Britain from an exporting nation to an importing nation.

Great Britain invested in other countries which at the time seemed well able to pay returns on foreign investments. However, foreign investing was carried so far with some countries that even with prohibitive tariffs they became unable to achieve a

sufficient excess of exports over imports for making the payments of income due to British investors, and repudiation followed in certain cases.

With goods and workers not allowed to move freely from one nation to another, a considerable change in the price level in terms of one currency can take place without corresponding changes in the price levels in terms of other currencies even though fixed exchange rates of the respective currencies are maintained. Higher relative prices in the debtor country naturally prove a handicap to the export of its goods upon which it must depend for making its foreign payments.

A demand for labour always accompanies the investment of new capital in any enterprise. So much foreign capital was invested in the U.S. for many years that there was not enough American labour to satisfy the demand, and therefore the U.S. placed no restrictions upon immigration. On the contrary, foreign labour was encouraged to come to the U.S. quite as much as foreign capital.

The immigration policy of the U.S. was a most important factor in keeping wages, and therefore prices, sufficiently low to permit U.S. goods to be sold freely in foreign markets. That policy permitted the industry of the U.S. to meet its obligations for the payment of incomes on the foreign capital invested, without stress. Any other immigration policy would have quickly checked foreign investing in the U.S.

Altogether many factors are involved which make the conditions surrounding foreign investing quite different from home investing.

There is now an unquenchable desire in each nation for the highest possible standard of living for its own workers, and each nation has immigration restrictions and tariff barriers for that purpose. As such restrictions interfere with the ability of debtors to make payments to foreign creditors, the best interests of all nations demand that in general each nation should cease allowing more of its capital to be invested abroad than the foreigner in turn invests in it.

Foreign Investing Injures Investing Nation.

It must be remembered that if a nation exports more than it imports, *the foreign buying power for its surplus products must come from the savings of its own people* in the long run. Great Britain, as a creditor nation, formerly sold a surplus of exports over imports through low wages and the *investment of savings* abroad. The U.S.A., while it was a debtor nation, sold a surplus of exports over imports through the *payment of savings* to foreigners on their investments in the U.S.A.

High standards of living are possible only as capital is expended in providing more efficient means of production. Investment in capital goods increases efficiency in the production of consumers' goods, and increases the amount of the latter available for consumption. If savings are invested abroad, the foreign consumer is benefited by an increase in the production and lower cost of consumers' goods.

Foreign investments become attractive because the workers at home have not received enough pay

to keep the demand for capital goods up to the home power to provide them. *Savings become available for improving the foreigner's standard of living, because the standard of living at home is below that justified by the productive capacity at home.*

Great Britain raised the standard of living in the countries in which she made her foreign investments. However, her contribution to the standard of living abroad was made through wages to her own people that held them in slums.

What is the motive behind foreign investing? Is it "raising the backward foreigner's standard of living," or is it profit? Even if it is the former, should not the wage and salary earners whose low pay makes the "noble deed" possible receive the credit, and should not their consent be obtained?

Certain nations have enjoyed higher standards of living because their natural resources attracted foreign capital. They have been benefited by capital investments at the expense of the standard of living of the country exporting the capital.

For any country to achieve the highest standard of living it must prevent leakage of its capital resources through foreign investment.

U.S. Profited by being Debtor Nation.

As stated in Chapter VI, the U.S. particularly profited from Great Britain's fallacious policy of investing her surpluses abroad. Some of Great Britain's early foreign investments were utilized in developing resources of the U.S. In later years

the increased production capacity which these investments had partly financed, coupled with the tariffs adopted by the U.S. to prevent a loss of gold, enabled the U.S. to enjoy an appreciable excess of exports of goods over imports.

The profits of U.S. industry sent as incomes to foreigners on their investments in the U.S. found their way back again for the purchase of U.S. goods. On account of the high amount of capital invested in efficient means of production, many lines in U.S. merchandise had but little competition in foreign markets. The industry of the U.S. prospered to such an extent that for many years there was a stress for more workers and immigration was stimulated. So far as international investments have been concerned, a nation's industry has been benefited by its being in the debtor position, providing it protected itself from the loss of gold so that it was enabled to enjoy freedom in the expansion of currency and bank credit for its needs under the gold standard.

The U.S. little realizes how fortunate she was under Great Britain's former management of the Gold Standard. In the zeal of British Bankers to make the Gold Standard work at all costs, they did not hesitate to cause disadvantages to the British people that became advantages to the American people. The British investments in the U.S., under the Gold Standard, enabled the U.S. to become equipped so that she could pay higher wages and still undersell at a profit in British markets and in markets formerly held by Great Britain.

Unbalance in Movement of Private Wealth from One Nation to Another should be Prevented.

In the best interests of all, international exchange transactions should be confined as far as possible to the transactions involved in the international trade in goods and services. By services is meant the accommodation afforded tourists, use of patents, copyrights, shipping, insurance, etc., but not loans and investments.

The ability of important sums of liquid capital to take flight through international exchange from a nation which is experiencing a lull in its commerce and industry, or because a boom is taking place in another nation, is an immediate serious disadvantage to the well-being of the nation losing the capital, on the gold standard or off. Stability is a prime essential if industry is to achieve the best results, and any changes which might not be immediately harmful, but which might later cause a reduction in the rate of industrial activity, should be avoided as far as possible.

No accommodation should be afforded by any agency of Great Britain for a flight to or from the pound, and other Governments should similarly protect their best interests. To frown at gambling in lotteries, sweepstakes, etc., and then permit sterling's exchange rates to be a plaything of international speculators is straining at a gnat. The private conduct of international exchange should be no more tolerated in any country than counterfeiting. It should be realized that the free movement of private wealth from one nation to another through

international exchange is just as harmful to the best interests of commerce and industry in peace time as it would have been during the War.

Each nation should enjoy to the utmost the ability to exchange its products for such products as it cannot produce as cheaply, and any interference in the natural parity of one nation's goods for another's, by the transfer of capital from one nation to another, should be tolerated as little as is possible. Regardless of the owners, the movement of capital from one nation to another should be subordinated always to the best interests of commerce and industry, exactly as the movement of goods and workers from one nation to another has been subordinated to the best interests of commerce and industry of the nations concerned.

A little consideration will reveal that with sound currency systems and low rediscount or bank rates prevailing in the more developed nations, there would never be any need of international investment and speculation between themselves, and that, so far as their well-being is concerned, they would not be harmed in the least if all such international investing and speculation were prohibited altogether.

An excess of capital leaving a nation over the capital coming in should be looked upon as a dead loss to a nation. While a nation allows its individuals to acquire wealth, the nation should take the view that as such wealth has been produced through the exploitation of its resources, *the possessor should be content to leave his capital in the country which produced it.* If the possessor wished to transfer his

capital to another country, then he should look up someone who wished to exchange wealth of the other country for wealth in his country. His country should not allow the export of capital without a corresponding import of capital.

The ease with which private wealth has been able to move from one nation to another has been a most serious basic handicap to a nation's continuous industrial equilibrium. If all privately-gained wealth had been denied the privilege of investment abroad, and had been compelled to remain in the nation which produced it, each nation's exports would have been kept in balance with its imports, and, in the development of industrialization, that distribution of its fruits which would have enabled the capitalists and the workers together to consume all they could produce would have been almost automatic. Any industrial disequilibrium would have been of short duration.

The ease with which private wealth has been allowed to move from one nation to another is the leak in the economic system which has caused the theories of many economists and the good intentions of many industrialists to go wrong. *The harm in permitting an "unbalance" in the movement of private wealth into and out of a nation cannot be too strongly emphasized.*

A great drawback of the gold standard has been the ease with which it lent itself to the investment abroad of surpluses created by an inequitable and unsound distribution of the fruits of industry in the investor's nation.

If the movement of private wealth through inter-

national exchange were prohibited, private wealth could be transferred from one nation to another through the transfer of goods. For a nation's best interests it should prevent leaks of this kind by making sure that all important shipments of goods leaving it were paid for through international exchange.

Investments in Undeveloped Countries.

With the international clearing association system in operation, and with sound currencies of constant purchasing power, many so-called primitive nations would be immediately released from their yoke of gold, and would soon become modern. Their desire for higher standards of living could then be translated freely into the development of more efficient means of production. Their need for better foreign-made tools would readily bring about an exchange rate for their currencies that would permit their products to be exchanged for the needed tools from abroad.

To the question: "How, with foreign investing stopped, is a backward nation ever to become modernized?" Japan and Russia provide the answer. Japan and Russia through their own efforts and without the aid of foreign investments have exchanged their raw materials for the tools and technical advice that have enabled them to make rapid strides in industrialization. What Japan and Russia have done other countries can do.

China under the correct economy could get the tools and technical advice for modernizing her

methods of production fully as fast as her people could learn to operate modern machinery and acquire tastes for its products. In a few years' time, under a rational economy, China could enjoy a standard of living approximating that enjoyed by the U.S. in the twenties and without the aid of any foreign investments in China.

There is no limit to the standard of living an intelligent people could enjoy under a rational economy and without the aid of any foreign investing and without any reduction in the standard of living of any other country. In fact, the contrary would be the case, no country could enjoy the highest standard of living without free trade, and no country could enjoy a high standard of living under free trade without benefiting the standard of living in all the countries having international commerce.

Many of the backward nations are in their present position partly because of the operation of the Gold Standard Economy which allows their resources in man-power and materials to be exploited to the advantage of capitalists. Goods and materials from backward nations are sold abroad, and often the profits are retained abroad.

The case of the development of an important resource in raw material in an undeveloped country which does not have the financial resources for its proper development should have careful consideration. The recent development of the copper resources of Northern Rhodesia offers a good example of such a case. When the possibilities of Rhodesia's resources in copper became known, it was evident that a large

amount of capital would be required to open them up on a scale that would make their development profitable, and it was, of course, also evident that the necessary capital was not available in Northern Rhodesia.

As the U.S. was the home of the copper industry, investors there were familiar with the possibilities from the development of copper prospects having the showing possessed by those in Northern Rhodesia. Therefore it was natural to turn to the investors of the U.S. for capital, though very little capital goods or consumers' goods from the U.S. were used in the Rhodesian copper development. Furthermore, the U.S. was a large exporter of copper, so that copper developments in Rhodesia are a menace to the prosperity of the copper industry of the U.S.

Northern Rhodesia is a crown colony of Great Britain and for this, and geographical reasons, the capital goods and the consumers' goods necessary to such a development naturally came from Britain. Also British capital, as well as U.S. capital, was used in the Rhodesian development.

Great Britain is an important importer of copper. For that reason the return of capital and the payment of profits to those entitled to receive them in Britain can be made without any transfer through international exchange, as the proceeds from the sale of copper in Great Britain will be available for making such payments. Thus the British investments in the development of Rhodesian copper were made almost directly with British goods, and the returns from those investments will be paid almost directly with a

Rhodesian product of which Great Britain is naturally an importer.

However, British capital was exported which might otherwise have been available for the construction of better homes and other facilities for the enjoyment of the people of Great Britain, for which there would have been a demand under the correct economy for industrialization. Also, the copper received as income on the British investments will continue to come year after year as a tribute from abroad, and will add to the excess of imports, already too large, which Great Britain is compelled to receive without any offsetting exports. On the other hand, however, the standard of living in Great Britain and the rest of the world may be raised through a greater amount of copper being available for use at a lower price. For such benefit, Great Britain and the U.S. have paid more dearly than the other nations.

The best interest of all countries, individually and collectively, would be served if each country developed its own resources in raw materials without the help of foreign capital, and practised free trade with the rest of the world.

In case, however, there is need of a raw material which is available in an undeveloped country, but for the development of which foreign capital is required, then naturally the capital should come from the country which will be benefited most, or rather, from the country which will be harmed least.

In some cases participation by several nations might be fairest to all concerned. Probably some years would elapse before the U.S., from the stand-

point of its best interests, could sanction the use of any U.S. capital in Rhodesian copper development. The world is fast reaching a stage in industrial development at which cases like that of the Rhodesian copper are rare, and even in that case there was no need of any great hurry about increasing the copper supply of the world.

The case of the Rhodesian copper development is only one of the many similar cases in which the U.S. participated.

For some years prior to 1930 particularly, the U.S. committed Great Britain's mistake of encouraging the investment abroad of profits accruing from an unsound distribution of the fruits of her industry, in the hope of avoiding injury to her foreign trade by the consequences of accumulating too much of the world's monetary gold. This had immediate beneficial effects, but the potential harm of such a short-sighted policy to the well-being of U.S. industry is now manifest, and will tend to continue as long as the U.S. remains materially a creditor nation in this respect.

Other Arguments Against Foreign Investing.

Mr. P. C. Loftus, M.P., in his book, *A Main Cause of Unemployment*, armed with the facts and the figures, draws a sorry picture of our plight, which largely resulted through the ease with which one nation could unsoundly become a debtor to or a creditor of another nation.

In speaking of the dilemma of creditor nations, he says—

They may receive the interest in the form of imports of goods and services. If they receive a large proportion of the interest in the form of imported food, it is obvious that they must damage their own agriculture and diminish the population on the land. (Great Britain is the only creditor country which accepts a large portion of the interest due in the form of imported food.)

If they receive a large portion of the interest in the form of manufactured goods, it must reduce employment in their own factories catering for the home market.

If they receive any of the interest in any kind of goods, it must damage and diminish their export trade for this reason. If the goods came in ordinary trade as imports, they would demand corresponding exports to pay for them: but coming in as interest, they are a tribute demanding no export of manufactured or other goods in return. Thus a direct cause of unemployment in creditor countries is the receipt of interest in the form of imported goods.

They may press for payment in gold, but there is not enough gold in the world, and the present scramble for gold by the debtor nations has already caused great economic distress to creditors and debtors alike.

In discussing the dilemma of the debtor nations, he says—

In many cases the debtor nation can pay the interest due if the creditor nation will receive goods in payment: if both the policy and the internal economy of the creditor country permitted the absorption and consumption of the debtor's goods to the full amount of the interest owed . . As the fierce struggle to obtain gold rises in intensity among the debtor nations, the value or price of gold also rises, and the price of all commodities keeps falling. The unfortunate debtor countries are placed thereby in an intolerable position. They contracted the debts chiefly when commodity prices were high, and the fall in prices accentuates the burden of the debt.

It has been suggested that if the War debts could be cancelled the situation would improve. Mr. Loftus points out that, ignoring previously defaulted international obligations—

The present outstanding commercial loans of Great Britain and the U.S. alone amount to nearly three times the amount of the outstanding War debts.

There is not enough gold in the whole world to pay for the foreign investments purchased by the citizens of the United States in the years 1919 *to* 1929.

It has been suggested that the present deadlock would be broken if the creditor nations would invest more in the debtor nations. This policy, Mr. Loftus warns, would be—

To add more and if possible larger doses of the very poison which has already nearly killed the patient.

Mr. Loftus tells of the evil consequences of easy borrowing by the newer countries, such as Australia, Canada, Brazil, the Argentine, Chile, etc.: first, loans for needed railroads, then loans for needed and not-needed extensions and other public improvements; then loans to repay loans, and next the loans to pay interest on former loans; then finally the scaling down of the principal amounts and repudiation, with serious losses to the creditor nation's investors, and says—

May it not be that the vast investments of capital in the new countries have actually retarded their proper development, and forced such development as has occurred either into wrong channels or too much in one or two directions? Would three-quarters of the Australian population be concentrated in the towns of that empty continent had vast British loans not been so readily obtained in the past?

If Great Britain's former policy of investing abroad, which was possible only through low wages to British labour, could have been pursued sufficiently far under low enough wages, the time would have come when the income from foreign investments would have

brought into Great Britain all the goods she could consume under the low wage system. There would have been no use for British workers in the production of goods, and they would have been forced to derive a precarious sustenance from services rendered to and gratuities paid by the moneyed classes.

If carrying foreign investing to an extreme would pauperize the labour of the investing nation, carrying it only a little way must be harmful.

If wages and salaries are not paid on a scale that will keep the consuming power of a nation in step with its productive power, surpluses will be produced. To ship the surpluses abroad on credit and then allow international investors to furnish the funds with which the foreigner pays for the surpluses, not only prevents the workers from enjoying the plenty which is produced at the time, but it is a short-sighted policy which in the past has brought more serious harm later through unemployment for labour and capital as well.

It is plainly evident that to carry on in the old way is but to make the situation worse. The fallacious practices of the past must be stopped.

The control over international investments is a responsibility which devolves solely upon the Government if any responsibility for the well-being of a nation in its international relations devolves upon it.

The evil consequences of past mistakes can be minimized only by adopting a sound currency and international exchange system, which will allow the economic forces within each nation to function in restoring a prosperity that will be lasting.

Reduction of the "Unbalance" in the International Investments of Individuals.

The return of capital to a creditor nation through international exchange would act so as to add to the foreign goods coming to it, and would thus accentuate the immediate handicap being suffered on account of the former departure of the capital.

In the present situation, the "unbalance" in *government* obligations which could be liquidated through an international clearing association operation, by the U.S. taking excesses of imports over exports and using *all* of the funds accruing to the Treasury's international exchange account as the result of such excesses, to reduce its tax burden, would be disturbing enough to its industry. But to bring about a balance in the international investments of *individuals*, through international exchange, would be far more disturbing to the industrial equilibrium of the U.S. Yet to let the present excess of such investments continue may be a menace to its future industrial equilibrium.

There is another angle to foreign investments. In the Great War, Great Britain sold U.S. securities formerly held by her nationals to buyers in the U.S. The proceeds from these sales were used by Great Britain to pay for war materials purchased in the U.S. Foreign securities may thus be converted into claims for goods in the debtor country by the creditor country. In a country enjoying prosperity a large conversion of its securities into claims for goods to be exported would be disturbing to its prosperity. With its capital and labour fully occupied in normal

production a demand for extra production would cause prices to rise or wages would have to be lowered to hold the general price level down to the level agreed upon as the standard.

In either event the standard of living of wage and salary earners and those who cater to their wants would have to be reduced while the "large conversion" of foreign-owned securities into claims for goods to be exported was in progress.

The incomes on foreign investments are not necessarily paid in goods to the creditor country. Often they are reinvested in the debtor country, and thus may not prove any hindrance to the trade of the creditor country at the time, but they would add to the excess of foreign investments of the creditor country, which might add to the handicap of its foreign investments to its foreign trade at a later period.

The truth is that foreign investments are unsound and are a menace to the equilibrium of a country's commerce and therefore its well-being regardless of whether it is debtor or creditor. In general, each country would be better off *if no profits were ever taken from its industry* either for investing in other countries or for paying earnings to other countries on their investments in it.

The problems involved in the present disequilibrium in international investments of the several nations require the careful consideration of their respective Governments. When a nation harbours individuals whose incomes from investments in foreign countries prevent it from deriving the benefit

of producing the full equivalent of all the goods consumed in that nation, its industry may not suffer much handicap, but the nation is deprived of the tax benefits arising from the industrial activities of which it is so deprived. For this reason it would seem that a nation which has an excess of foreign investments is thoroughly justified in levying additional taxation on incomes from foreign investments, as suggested in Chapter VIII, which would tend to bring about a balance in international investments.

With an international clearing association operating and confining its transactions to the best interests of international trade in goods and services and the sound liquidation of the international obligations of Governments, as it should, and with a pressure to reduce the disadvantage of the "unbalance" in the international investments of individuals through the taxation of foreign incomes, there would be an economic force operating to reduce the "unbalance." This would cause the foreign investments held by individuals of a nation which is a creditor in this respect to be at a discount compared with the property and securities of their nation, which have the same earning power. With prosperity restored to all nations, many foreigners now residing in creditor nations would take advantage of this situation, and would exchange their property and securities of the creditor nation for the securities of their own nation, and then return to their own nation, taking its securities with them. Also, others would emigrate to a debtor nation, taking securities of that

nation with them. By such transactions, the "unbalance" would be reduced, thus reducing the creditor nation's excess of imports of goods over exports, and thus reducing the possibility of a disturbance to the industrial equilibrium of a debtor country by a large conversion of its foreign-owned securities into claims for its goods to be exported.

A nation's best interests would demand that it allow no disturbance to its commerce and industry by the transfer of the capital of individuals through international exchange. With care, the hardship to the owners of foreign investments in reducing the "unbalance" need not be serious. In many cases the losses incurred would be small compared with the losses which now seem to confront many owners of foreign investments, through the present seeming inability of the nations in which they have invested to make payments.

"Unbalance" in the International Investments of Individuals Not Vital Issue Now.

While we are in the present muddle created by unsound currency management and unsound practices in international exchange, the disorganizing effects of the War debts and the disequilibrium in international investments seem like mountains. They would appear only as molehills in any nation if it would awaken to the gold fallacy, and take the simple steps required to put its monetary system on the sound basis that would permit its industry and commerce to function in casting off depression.

While there need be no hurry about trying to reduce the present "unbalances" in international investments, it is important to recognize that such "unbalances" were brought about by unsound practices in the past and that similar unsound practices should not be permitted in the future.

CHAPTER XI

LASTING WORLD PEACE—CONCLUSIONS

BEFORE the War the development of the gold standard, to meet the needs of modern commerce and industry, had progressed to the extent that each nation had its central or government bank in which was deposited much of its monetary gold. Bank cheques and bank-note currency fulfilled the needs of domestic commerce, and gold was being used more for paying the balances in international exchange.

In a more developed nation, experiencing no serious international stress for gold, a credit currency based upon the central bank loaning credit or currency to other banks, against certain government obligations and short-term obligations of commerce, adequately fulfilled all the internal needs of commerce for currency. The way such currency could be automatically expanded or contracted to suit the needs of commerce and industry seemed to make it the ideal. But the entangling alliance made between it and gold was its weakness, for when a nation's gold reserves commenced to be depleted, that nation often resorted to the fallacious one-way acting high rediscount rate and brought upon itself the misery of deflation, while a nation whose gold reserves tended to increase enjoyed the advantages of a plentiful supply of money.

Cause of War—Gross Injustice of the Gold Standard to Debtor Nations.

Generally, under the gold standard, prosperity ruled intermittently in the nations which were creditors in the international trade of goods and services, and depression ruled continually in the nations which were debtors in this respect, and it was obvious that to enjoy any prosperity a nation must not have unfavourable international trade balances; it must have plenty of gold.

The seriousness of being in the debtor position under the gold standard has long been realized, as a number of nations remain backward that would be modern but for their inability to extricate themselves from a serious debtor position. They are held in bondage by allegiance to a monetary system which renders them impotent.

The decades preceding the Great War were characterized by pressure in the more developed nations for foreign trade and the avoidance of the evil consequences of unfavourable trade balances. One nation was quick to accuse another of dumping, and when one nation imposed a tariff barrier for its protection, this was sometimes looked upon almost as an act of war by another nation having its foreign trade disturbed. Covetous eyes were cast upon territories which appeared to have resources capable of producing favourable trade balances through exploitation or which appeared to have possibilities of increasing the free trade area of some other country. Displays of military and naval strength were made before distressed debtor nations in the

interests of the gold lenders of creditor nations. As they were powerless to improve matters, such conditions were exasperating to the executives charged with the responsibility for the well-being of their respective peoples, and such conditions bred international friction and discord.

It requires no stretch of the imagination on the part of those familiar with the underlying causes which had been brewing through the preceding years to realize that the Great War itself was brought on as a result of the operation of the gold standard, which caused the pernicious international rivalry for favourable trade balances and gold. *The God of War himself could not contrive for the world a monetary system better suited to his purposes than the gold standard.* Any efforts to bring about permanent world peace, while international monetary practices clash with the first law of nature, are founded upon shifting sands. Our attempt to retain the gold standard and liquidate the debts of the Great War, which was the havoc of the gold standard's shortcomings in the first place, will appear grotesque to future generations.

A Sound Economy and War.

Economic dissatisfaction has been a background of most international conflicts and most internal dissensions and revolutions, "bloodless" and otherwise. With currency units of constant purchasing power, and with a sound international exchange system which would make absolutely free trade a reality, a little consideration will reveal that the

economic well-being of any particular group of people could not be improved in the least by any possible result of war. If, as the result of war, the State of California with its many resources became a British possession, the people of the British Isles could not permanently and equitably benefit economically beyond what they would benefit from absolutely free trade with the State of California. With the State of California using British money, the development of resources of California might appear attractive to British investors as an outlet for their surpluses, but it must be remembered that if Great Britain were pursuing the correct economy—the economy best for the people living in Great Britain—there would always be a demand at home for all the available capital, and no capital could be invested abroad without reducing the standard of living of wage and salary earners and those who cater to their wants, living in Great Britain. A war indemnity from the conquered would require production by the victor to be less than its consumption, which might not prove an unmixed benefit. Under a sound international exchange system, the only possible permanent economic benefit to the masses of Great Britain, from the State of California becoming British, would be the possibility that with a larger area to administer, the cost of administering government *per capita* might be reduced.

With sound currency systems and a sound international exchange system, the various nations would normally enjoy continuous prosperity under free trade, and would prefer not to disturb the enjoyment

of their prosperity by engaging in war. However, in case a nation for some not now explainable cause, became involved in war, the consumption of peace-time goods would have to be curtailed, in order that the nation's energies could be devoted to prosecuting the war. That could probably best be accomplished by levying higher taxes on all incomes. This would enable the Government to pay for the war, as it progressed, from taxes, rather than to owe its cost, when it was over, to those who stayed at home and invested in war loans from the large surpluses accruing to them during the conflict, as happened in the last War.

The fact that during the last War the standards of living of the industrial workers improved when a large part of their production was consumed on the battle-fields, and by those engaged in war activities who gave no goods in return, is surely a sad reflection upon the economic system prevailing previous to the War.

Some have mentioned the loss of capital in the prosecution of the War as the cause of the present depression. A nation that financed its war activities without borrowing more from abroad than it lent abroad did not lose capital. True, its public debt may have been increased, but by a corresponding amount certain of its own people became creditors. In general, in those nations which did not borrow from abroad, the cost of the War was financed in the main out of the prosperity prevailing during the prosecution of the War. Owing to the healthier condition of her industry during the War, the U.S. emerged much wealthier than when she entered.

The experience of the U.S. and the experiences of other nations in the War serve to emphasize the tremendous advantages, under industrialization, accruing from maintaining the power to consume in balance with the power to produce.

The War demonstrated that credit currency unfettered by gold is undeniably sound, and when its purchasing power is regulated to a constant price level by the only means possible—intelligence in the regulation of the general wage and salary level—it will prove the greatest aid ever invented for man's material well-being, and is bound to be the enduring currency system of the future. The use of such a currency would automatically bring about that equity in the distribution of the fruits of industry, and that balance between the power to consume and the power to produce, that would enable industry constantly to function at its best.

As the desire for goods is practically insatiable, with a balance between the power to consume and the power to produce, which would enable industry to be constantly functioning at its best, the production of goods and the ability to enjoy goods could be limited only by the desires and inventive genius of man.

The present difficulty of repaying international loans under the gold standard has been sufficient to demonstrate the futility of loaning to a warring nation.

"In 1795 Austria raised the first war loan. It was floated in England. The sum was £4,600,000—an amount unprecedented in those days. The loan was opposed unavailingly at the time by Fox. For three

years Austria made her half-yearly repayments. Then nothing more was paid. On the contrary, fresh advances seemed necessary, on account of Austria's gold shortage, and were made, and by 1823 the British claims on Austria amounted to £15,648,730. The British Government of the day settled this war debt for £2,500,000, or roughly three shillings in the pound."

Under an international clearing association operation, a nation would be dependent upon its own resources for the sinews of war as other nations would not be much interested in making a loan to it, which could be repaid only by goods at a later date.[1] With foreign loans becoming unattractive to the lending nation, a nation engaged in war would be forced to continue exporting as much as it imported, otherwise the exchange rates of its money would fall and render importing impracticable.

If a nation wished to assist another nation which was at war, the Government of the former could extend credit to the warring nation for goods and services. The assisting nation, in order to maintain its general price level steady and to finance soundly the assistance it gave, would have to levy higher taxes and thus reduce its standard of living while it was rendering such assistance. When the war was over its standard of living could be correspondingly raised while the warring nation was paying off its debts, as is suggested on page 285.

To render assistance and be repaid for it in this way would be disturbing to the well-being of the

[1] This view has prevailed in connection with the Italy-Abyssinia War under the gold standard even.

assisting nation, and only a nation feeling a strong moral obligation could afford to make the sacrifice.

Enlightened thinking to the extent that we were emancipated from gold fetishism would not only prove a great forward step in removing the cause of war, but it would prove a very important step in hindering the prosecution of war.

With the various nations practising an economy which kept their power to consume in balance with their power to produce, and which kept their exports in balance with their imports under free trade, the outbreak of a war between two important nations would be disturbing to the balance in the foreign trade of most of the others, and there would not be any compensating advantages economically to any of the nations. Therefore, if a war were threatening between two nations, all the others would be zealous to prevent it in order to avoid any dislocation of their own commerce and disturbance to their own prosperity, if for no other reasons.

The adoption of a sound monetary system, with a little intelligence in international exchange, would automatically replace international rivalry and friction by international co-operation and goodwill. Any attempt to abolish war without abolishing the monetary system which prevents the practice of "live and let live," between nations, is doomed to disappointment.

The way to lasting World Peace is through an exchange system which will permit prosperity and the great mutual advantages of free trade. Then territorial expansion would prove an economic handicap

rather than an advantage to the masses of every nation.

Only through the practice of the economy which would tend to make a country immune from war can it develop the highest productive power, and therefore the highest defensive power should it ever become involved in war.

The question of lasting World Peace is a problem in Currency and International Exchange rather than a moral question.[1]

CONCLUSIONS

It is time we more fully realized that our economic well-being is controlled absolutely by economic forces as real as any forces in nature, that depression is not a mental condition to be dispelled by hypnotism or "hokum," and that our economic forces are of our own making and always 100 per cent responsive to our economic conduct. We should harness by precise control the economic forces which determine our well-being, and utilize them for our benefit, instead of allowing them to run wild. Prosperity is dependent solely upon the exercise of intelligence in our economic conduct.

[1] Nothing gained by war between nations is ever worth the cost and sacrifices. The economic causes of international friction should be removed and the possibility of war as a means of securing international justice should not even be thought of by those entrusted with international responsibilities. A reputation for fair dealing should be the goal of all negotiators in international problems, however powerful their countries may be.

An entangling alliance may encourage a quarrelsome small brother to take advantage of his position. Collective security may place burdens and sacrifices upon a nation which is in no way responsible for a dispute between other nations.

Small civilized nations have done very well under the policy that they alone must bear the penalty of their own international misconduct.

In the present situation most nations have an abundance of liquid capital, facilities for production, and certain raw materials. Each nation has an abundant power to produce, but, in order to restore its prosperity, each nation is in desperate need of a power to consume all that it can comfortably produce.

We have idle capital and idle labour simply because an economic force as real as any force in nature has weakened the natural attraction between idle capital and idle labour. Intelligent investors are unable to find profitable employment for their capital and thus give employment to labour simply because the power to consume has fallen out of balance with the power to produce.

Heretofore two systems have been used for matching a nation's power to produce with a power to consume. In one system, which may be designated the low-wage system, a nation is dependent upon a power to consume from abroad along with its own to match its power to produce. This system, to function for any time, requires an excess export of goods over imports and the investment abroad of surpluses derived through the denial of purchasing power to the workers at home—purchasing power which would keep the home power to consume in step with the home power to produce and which would ensure prosperity for all.

This system is fallacious, and can bring only a temporary prosperity as we have observed, because practising it for a time brings income from the foreign investments, and an excess of foreign income prevents

a nation from enjoying the exercise of a power to produce, even equal to its own power to consume.

Furthermore the workers realize that the efficiency of production is constantly advancing and that therefore their standard of living should be constantly advancing and never falling, and the dole and collective bargaining enable them to forestall reductions in wages.

Heretofore, under the gold standard economy, a nation has limped out of depression by reducing wages so as to undersell in more prosperous nations, but this system is of no avail now, because the leading nations are equipped for volume production, and all are suffering from the same malady—depression. Each has placed tariff barriers to prevent the loss of its own buying power to other nations.

The conditions favourable to prosperity through the low-wage system have passed for all time. Now each nation is dependent solely upon a consuming power within itself for restoring and maintaining its prosperity.

The other system, which may be designated the high-wage system, requires that increases in wages keep pace with improvements in the efficiency of production, so that the purchasing power of the masses can be utilized for keeping the power to consume in balance with the power to produce.

The Gold Standard is Totally Unsuited to the Needs of the Machine Age.

If a nation would rid itself of depression for all time it must first emancipate itself from the gold

fetish. Also it must realize that raising wages—not lowering wages—is the cure for unemployment of labour and unemployment of capital.

The gold standard broke down because it could not cope with the international debt situation which its use permitted to be brought about, and because of that situation it cannot be restored again without very serious conflicts in the interests of the nations involved. While the currencies loose from gold have depreciated in gold value, the nations off the gold standard realize that the values of their currencies are still too high, in terms of goods, for their prosperity, i.e. their price level is too low.

In any attempt to get the nations off the gold standard on again, each would seek to reduce further the purchasing power of its currency, and each would strive to have its currency unit set at a relatively lower gold parity than the others, so as to ensure it against the possibility of an unfavourable balance in trade. IF the conflict of interests could be bridged by what, at the very best, could be only makeshift compromises, and IF the War debts could be cancelled, the "unbalance" in international investments and other obligations is so serious, and the desire in each nation for a currency management which would permit prosperity is so urgent, that the question naturally arises as to *how long* would or *could* all hang on to such a fluctuating and unscientific standard of value.

As stated previously, the opportunity for prosperity under the low wage system has passed for all time and prosperity is possible only through high

enough wages and salaries to permit a balance between consuming power and productive power.

To have continuous prosperity under the latter condition requires the following—

(*a*) A currency unit of constant purchasing power.

(*b*) The proper balance between the export and import of goods and services without putting the workers of a country having a high standard of living in competition with the workers of a country having a low standard, and

(*c*) No loss of consuming power or potential productive power through foreign investments.

The gold standard is a stumbling block to the stability of prosperity under the high wage system because its use interferes with the attainment of each one of the three fundamental requirements for a constant balance between the power to consume and the power to produce.

During the past years the people of all nations have suffered untold injury from trying to adhere to the gold standard with fixed gold parities for their respective currencies. In spite of this many are advocating a return to that system, but the great obstacle to its adoption again is "once bitten twice shy."

To try to restore an antiquated yardstick of value which varies so much that at times it has to be abandoned to avoid disaster under it, is wasting time that should be devoted to evolving a standard suited to the needs of the Machine Age.

Until we avail ourselves of an unvarying yard-stick of value, by the only possible means, we need

not wonder that the science of political economy is now so inexact, that so many of its tenets seem to fail in practice, and that there is so little agreement among its high priests. Naturally, without a fixed datum line or an unvarying unit for valuing the forces involved, theorizing about factors—all of which are variables—becomes almost fruitless, and it is not surprising that agreement among economists is rare and that effects are often mistaken for causes.

The gold standard was successfully operated only when its manipulators had the power to lower prices and wages through deflation and the ruination of debtors and many creditors as well, and through the misery of unemployment.

It has become plainly evident that the tendency in industry is always towards higher efficiency in production and that therefore the buying power of the workers should be continually rising and never falling.

With the inauguration of the dole, and collective bargaining, labour is no longer compelled to take lower wages or starve, and therefore the day for the successful operation of the gold standard with its inherent gross injustices has passed.

Gold as a standard of value is so totally unscientific and unsuited to present-day needs that, fortunately for the future, intelligence is likely to prevail to the extent that the gold standard will never be restored.

Many orthodox thinkers who labour in the fog of the gold standard economy blame the inflexibility of wage rates for the depression. They would have

the workers take lower wages and allow prices to fall with every rise in the demand for the non-essential commodity, gold. They would have debtors ruined and the whole internal economy of a country upset to compensate for the offences of international speculators and investors against sound economic law. Instead of man's being master they would have him mastered by gold fetishism. They would have man made for money and not money for man.

On the whole, gold fetishism has been far more devastating to human happiness than witchcraft, and the future is bound to rate both on about the same level.

There can be no banking in harmony with the public's best interests while book-keeping entries of credits and debits at the banks have any particular connection with gold or any other commodity which would in any way limit the ability of bankers to expand bank credit or in any way make book-keeping entries at the banks subject to supply and demand.

As will be gleaned from Chapter VII, the work of banks in the main consists in recording debts incurred by individuals and making them the basis of bank money which is credited to other individuals by book-keeping entries.

A better plan for accommodating the needs of commerce and industry with the right amount of money at all times is impossible. Whether or not labour and capital are fully employed and not the amount of gold hidden away in vaults, should be the only consideration for determining the "right amount" of money available for use.

Under a rational banking system: (*a*) There would be no restriction on the short-term money available. Supply and demand would have no bearing upon the banks' ability to make book-keeping entries for short-term bank money. (*b*) When labour and capital are comfortably employed only savings should be available for long-term borrowings. Normally the ability of bankers to expand bank credit safely for long-term use should have no bearing upon the bank credit available for long-term employment.

Supply and demand for bank money should have no consideration in determining banking policy. Banking—the recording of debits and credits by book-keeping entries—is a public service, and banking policy should be dictated wholly by the best interests of the public, as pointed out in Chapter VII.

Economic Forces as Real as Any Forces in Nature.

Many orthodox thinkers complain that because of man's changing moods and habits there can be no safeguard against periods of prosperity followed by periods of depression.[1] However, there are certain fundamentals in man's nature *which can always be relied upon* to determine his economic conduct and which may be mentioned as follows—

[1] Prosperity was never followed by depression because of any change in man's fundamental desire to consume. Depression has always been brought about through a disequilibrium between consuming power and productive power, which has generally been accentuated by a deflationary monetary policy.

To contract the volume of money available to commerce does not change man's desire for a high standard of living, it forces a lower standard of living upon him by restraints as real in the economic sphere as shackles are in the physical sphere. When commerce and industry have once become accustomed to a certain volume of bank money, a worse economic crime against society than contracting that volume is impossible.

(*a*) After having enjoyed a certain standard of living man will move to a lower standard only very reluctantly.

(*b*) The desire for a higher and higher standard of living is universal and no nation can ever produce by the most efficient organization possible the equivalent of more than its people would like to produce and consume.

(*c*) Security is a prime essential to the enjoyment of higher and higher standards of living. (Incidentally, security is one of the greatest factors in human happiness.)

(*d*) The profit motive is inherent in human nature and capital will not remain idle and cause idle labour so long as there is profitable employment available to capital.

In an economy which will allow the above fundamentals in man's nature to function freely and logically, economic forces will prove as real as any forces in nature, and calculations based upon them will become quite as dependable in the economic world as those based upon the force of gravity in the physical world.

The foundation of that economy is a currency unit of constant purchasing power at the right level under free competition, *by the only possible means*—the Government control of the general wage and salary level. A rational control of its exchange rates, a rational control of bank credit, and a rational pension system are also essentials for the best results.

A steady buying power of money under free competition rules only when there is equilibrium between

consumption and production, and *vice versa*. The degree of prosperity ruling depends upon the degree of balance between consuming power and productive power. As wages determine costs and therefore prices in the main, and as wages determine consuming power in the main, prosperity can rule only if wages and salaries, the consuming power of the consuming masses, are kept adjusted to the correct level.

Whether depression or prosperity rules depends upon wages.

We are inclined to think that practices to which we are accustomed are natural and that any new practice would be artificial. Maintaining a currency unit of constant purchasing power by the Government's controlling the general wage and salary level, which would automatically maintain the power to consume in balance with the power to produce, would be a man-made measure beyond question, but it would be eminently fair to all and thoroughly effective for the end in view and therefore sound.

Investing gold, one of the many commodities, with a fictitious importance and making it a standard of value; tying a banknote currency to gold at a fixed parity and *fixing* its exchange rates with other currencies; and juggling with the volume of central bank credit and currency outstanding in an effort to control indirectly the general price level—are all artificial practices also, but highly fallacious because they fail signally to provide a money system which will enable the possibilities of the Machine Age to be realized.

In the nature of things, an instrument worthy to be called money must be man-made, and it is the part of wisdom that it be given an unvarying value at the right level *by the only possible means* directly, and in plain view of all.

Reverence for inflexible exchange rates and the quantity theory of money for controlling prices is orthodox fog which must be cleared away before any worth while prosperity and lasting world peace are possible.

Lasting Prosperity and Peace within Easy Reach.

Straight-thinking people of Great Britain long ago recognized the far-reaching advantages and fundamental soundness of Free Trade. Also they recognized the advantages and fundamental soundness of private enterprise and the pricelessness of economic liberty, and they recognized that economic liberty is impossible without free competition and the non-interference by the Government with supply and demand.

It is for the straight-thinking people of to-day to recognize that Free Trade is possible and can prove a blessing to all only if the benighted reverence for inflexible exchange rates is overcome. It is for them to press for a business-like management of sterling's exchange rates to the end that British exports will be kept in balance with imports without any tariffs.

It is for the straight-thinking people of to-day to recognize that free competition can be a blessing to humanity only if consuming power is kept in step with productive power. It is for them to recognize

that the general wage and salary level determines the balance between consuming power and productive power and determines the buying power of sterling. It is for them to realize that whether depression or prosperity rules depends upon wages and that the "dispute method" of adjusting wages is altogether too crude for any success in the Machine Age.

It is for the straight-thinking people of to-day to interest Parliament in a business-like control of the general wage and salary level to the end that the general price level of 1928 will be maintained firm under free competition. If they will, then no matter how quickly Parliament responded, prices would harden before it could act, and industrialists throughout the country would be laying plans for improving and enlarging their facilities of production. Before the first Government decree for a rise in wages and salaries could become effective, depression and want in the midst of plenty would have become a pestilence of the past. Prices would be up, profits would be rolling in, and full employment for capital and labour at healthy profits and wages would be ensured to the end of time.

Furthermore, Great Britain, by demonstrating the only way a country can enjoy a consuming power in constant step with its full productive power, and under economic liberty and free trade with all the world, would contribute the greatest forward step to lasting World Peace in all History.

By a few simple acts of its own Government each country could quickly free itself from depression for all time. For a government to blame the acts of

other governments for its depression is orthodoxy and is about as useful as blaming the inhabitants of Mars.

No International Understandings Needed in Beginning.

Fortunately, no international understandings or agreements are necessary or even desirable at first, for bringing about a lasting prosperity to each individual nation, and for making the great step forward to lasting world peace. When some progress has been made by the only sound means in casting off *the depression which has resulted from the practice of the gold standard economy*, the advantage of an international clearing association would soon become apparent, and a little international co-operation in bringing it about should prove an easy and logical step. Under the international clearing association plan proposed, the more selfishly each nation strove for its own best interests the better it would prove for all.

If intelligence can be exercised now in bringing about a sound solution of our present serious tangle, we can all soon be enjoying a prosperity and a degree of security against war such as has been only dreamed of in the past, and future generations will wonder at our stupidity in being so deluded by gold, which has caused so much human suffering through external friction and war and through internal maladjustments and want.

As suggested in the beginning, the symptoms of depression are numerous and involved, and therefore

we think that the cause is involved and requires an involved cure, whereas the measures necessary for affording lasting prosperity and world peace are so few, so simple, and so equitable from every standpoint, that even the man in the street will later wonder how their effectiveness and practicability could ever have been questioned.

APPENDIX

CURRENCY UNIT OF CONSTANT PURCHASING POWER IN SPECIAL CASES

It may be of interest to consider how a currency unit of constant purchasing power would work in an unindustrialized nation. As an extreme case in one direction, let us consider a country where the peasant view dominated and where each individual worked for himself and where no one worked for wages in the production of goods or services. Some individuals could work alone while others might join together and specialize in the production of a particular class of commodities or services, each participant being a partner and sharing in the profits, though not receiving any remuneration in the form of wages. The various commodities or services produced in such a country would find their natural parity with each other.

With no wages being paid, except to, say, government employees, the purchasing power of such a country's currency for its own products would not tend to vary much, if the only taxes levied were upon incomes, and if its currency were managed so that there was a good margin of credit currency or central bank credit always outstanding which bore a rediscount interest rate.

In case there was a tendency for the purchasing power of the currency to change, the *quantity theory of money* might work perfectly in a country where

no wages were paid in the conduct of its commerce and industry. A rising tendency in commodity prices would be corrected by a higher bank or rediscount rate for currency or central bank credit, while a falling tendency in commodity prices would be corrected by a lower bank or rediscount rate or by the payment of a few government obligations, by an issue of "printing-press" currency instead of by levying taxes.

With the exchange rate of such a country's currency regulated so as to keep its exports balanced by its imports, its currency's purchasing power for foreign goods would vary only as the value of the classes of goods it produced varied with the value of the classes of goods imported. As the natural parity of one class of goods with another class does not tend to vary much, and as the country would be limited in the goods it could export by the goods it could import, the purchasing power of its currency for goods produced at home or abroad would tend to vary but little on the whole.

As an extreme case in another direction, suppose a country had no other industry but the mining of coal, and that it was dependent upon the outside world for all other commodities consumed in it. Its currency would be regulated to a constant purchasing power for the commodities consumed in the country by the regulation of the general wage and salary level, and the exchange rate of its currency would be regulated to keep its exports balanced by its imports.

If the prices of the commodities consumed tended

to sag below the level adopted as the standard, then raising wages would tend to increase the cost of producing coal, which would tend to reduce the amount of coal that could be shipped abroad. Such a reduction would result in the exchange rate of the currency of the coal-producing country being lowered. This would increase the cost of imports to its consumers and would thus raise the general level of prices to the level adopted as the standard.

In case higher wages did not correspondingly raise the cost of producing coal, then the higher wages and salaries would increase the buying power of the workers, and would increase the consumption of the commodities imported. In this case, to keep the country's exports balanced by its imports, the exchange rate of its currency would also have to be lowered, and this would also increase the cost of goods imported and thus raise the prices of commodities to the level adopted as the standard.

In a similar way, if the prices of commodities tended to be above the level adopted as the standard, lowering the general wage and salary level would result in lowering the prices to consumers of the goods imported, and thus restore commodity prices to the level adopted as the standard.

Consideration will reveal that as long as there was a free market for coal, and as long as the purchasing power of the coal-producing country's currency was regulated to a constant level by regulating the general wage and salary level, and the exchange rate of its currency was regulated so as to keep its imports balanced by its exports, the prices of coal and wages,

if the law of supply and demand was allowed to operate freely between them, would adjust themselves so as to keep the producing power of the country in constant balance with its consuming power. Also careful consideration will reveal that by closely regulating the coal-producing country's currency to a constant purchasing level and by regulating the exchange rate so as to keep its imports closely in balance with its exports, its inhabitants would be enabled to enjoy a maximum of imports continuously.

INDEX

MADE IN GREAT BRITAIN AT THE PITMAN PRESS, BATH
C6—(C.217)